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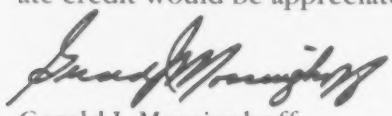
PMA
STATISTICAL FACT BOOK
December, 1987

Foreword

This publication is a reference guide to the prescription drug industry. It provides some of the key data that describe the operations of the U.S. pharmaceutical industry and the context in which it operates.

We welcome comments on this publication and inquiries for further information. We encourage reprinting of the contents as necessary; appropriate credit would be appreciated.



Gerald J. Mossinghoff
President

December 1987

The Pharmaceutical Manufacturers Association

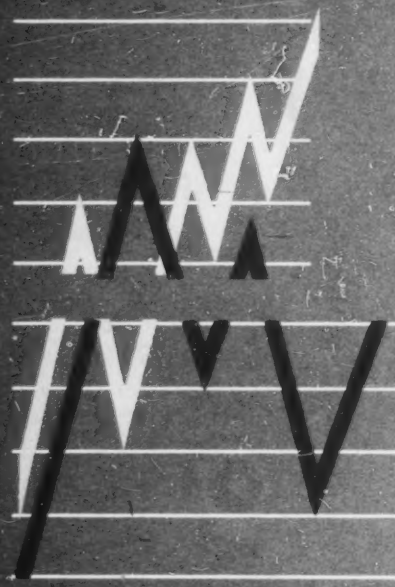
The Pharmaceutical Manufacturers Association is a nonprofit scientific, professional and trade organization of more than 100 firms that discover, develop and produce prescription drugs and biological products in the United States. The Association's members produce more than 90 percent of the prescription drugs used in the United States, and about half the free world's supply of prescription drugs. Worldwide pharmaceutical sales of PMA member companies in 1986 totaled an estimated $36.1 billion. PMA members spent $4.6 billion worldwide in 1986 to research and develop new pharmaceutical products.

The mission of the research-based pharmaceutical industry is to satisfy public demand around the world for medicines of the highest quality. To accomplish this mission, firms in this industry discoyer, develop, manufacture, and market ethical pharmaceuticals, biologicals and diagnostic products. They place special emphasis on innovation and quality, and are committed to supporting comprehensive research and development programs leading to products and services used in the prevention, diagnosis, cure and treatment of disease. As investor-owned private enterprises, pharmaceutical firms seek reasonable returns on their substantial and high-risk investments in research and development.

The Pharmaceutical Manufacturers Association was founded in 1958. It is the successor to the American Association of Pharmaceutical Chemists, organized in 1907 and renamed the American Pharmaceutical Manufacturers' Association in 1922; and to the National Association of Manufacturers of Medicinal Products, founded in 1912 and called the American Drug Manufacturers Association after 1916.

The Pharmaceutical Manufacturers Association is governed by a 36-member Board of Directors that establishes the policies carried out by its staff and sections. The Association has 13 functional units known as sections; these are composed of representatives of member firms who work closely with the Board and staff on numerous projects. The sections are Production, Engineering and Materials Management; Research and Development; Quality Control; Biological; Marketing; Medical; International; Public Affairs, Financial, Law, Personnel; State Government Affairs; and Washington Representatives.

Pharmaceutical Manufacturers Association



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I. An Overview Of The Pharmaceutical Industry In The U.S.

The research-based pharmaceutical industry is one of America's most important high-technology industries. The creative contributions of the industry add immeasurably to the quality of life of people worldwide.

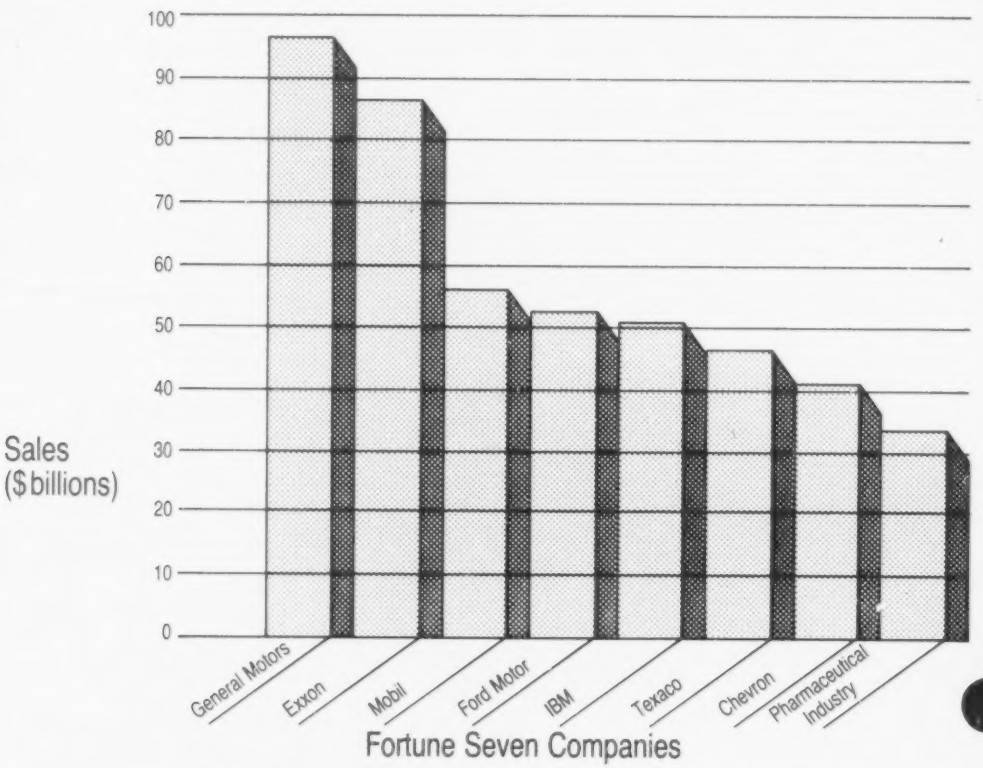
This relatively small, competitive industry also makes major contributions as an industrial entity:

- It is a steady employer of more than 300,000 skilled and productive individuals who are located in facilities throughout this country and the world.
- It leads the world in total sales of pharmaceuticals.
- It pays one of the highest effective federal tax rates of all industries.
- Unlike many other U.S. industries, it has a favorable balance of trade.

A Relatively Small Industry

Compared to other major U.S. industries, the pharmaceutical industry is relatively small. In 1985, total worldwide sales of PMA member firms were $32 billion, making the entire industry smaller than any of the first seven companies on the Fortune 500 list.

Sales Of The Fortune Top Seven Companies Compared To Sales Of The Pharmaceutical Industry, 1985

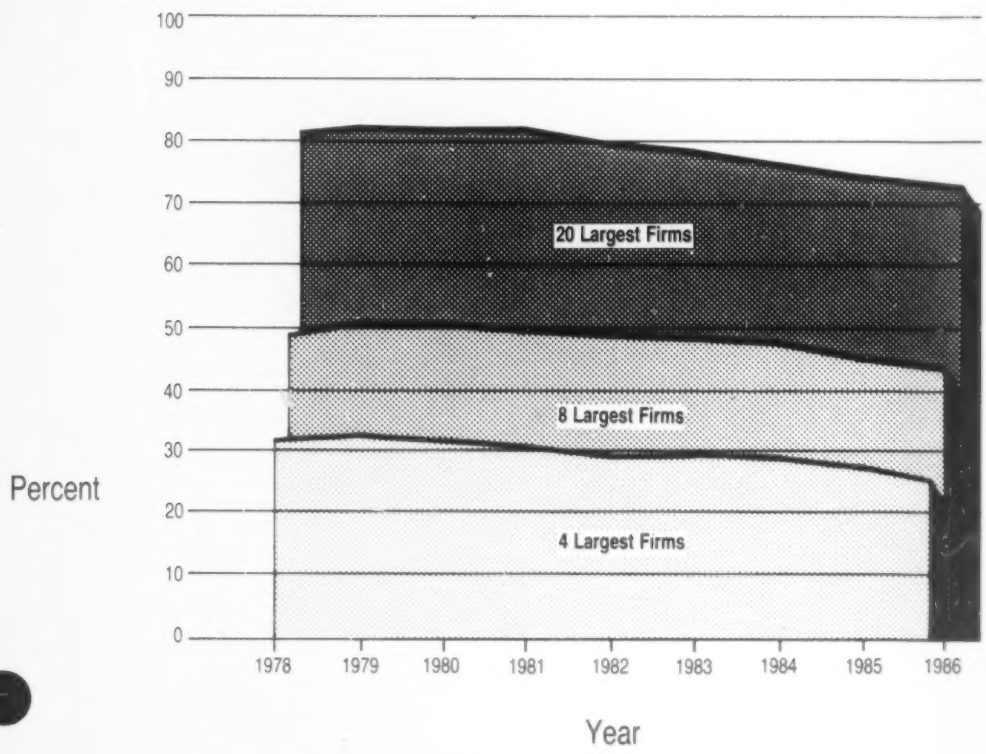


Source: Fortune Magazine, April 28, 1986, p. 182.

The Industry Is Highly Competitive

The pharmaceutical industry is highly competitive. The share of total sales held by the four largest firms accounts for only 25 percent of industry sales; the top eight firms account for less than 50 percent of the market. Not one of the major companies holds more than a 7 percent share of the market.

Concentration Ratios For Firms Measured In Total Prescription Dollars 1978–1986



Source: National Prescription Audit, IMS America, Ltd.

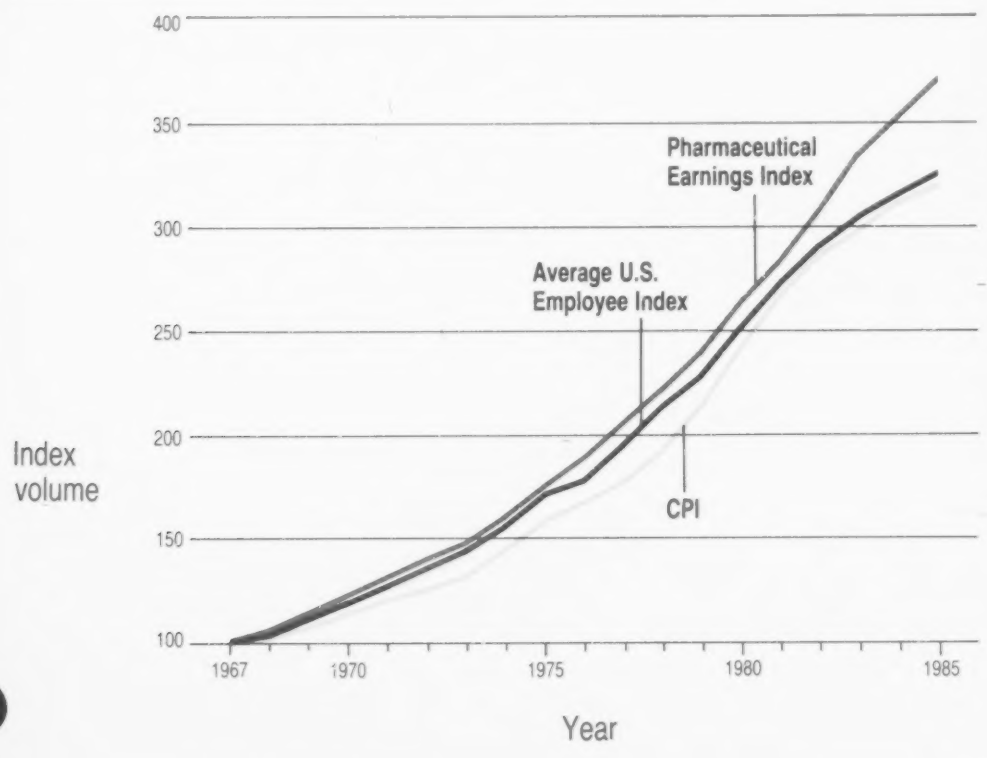
An Industry That Contributes To The Nation's Economy

- As an Employer
- As a Producer
- As a Taxpayer
- As a Trading Partner
- As a Distributor

The Industry's Contribution As An Employer . . .

Unlike some American industries in the 1980s, employment among PMA member companies has been growing. In 1985, 312,400 people were employed in the pharmaceutical industry compared to 306,400 in 1980. The pharmaceutical industry has consistently increased the wages of its production workers at a higher rate than the rate of increase in the Consumer Price Index, meaning they receive real growth in their wages.

Index Of Hourly Earnings For Production Workers In The U.S. Pharmaceutical Industry And The Consumer Price Index, 1967–1985 (1967 = 100.0)



Source: Bureau of Labor Statistics, 1987

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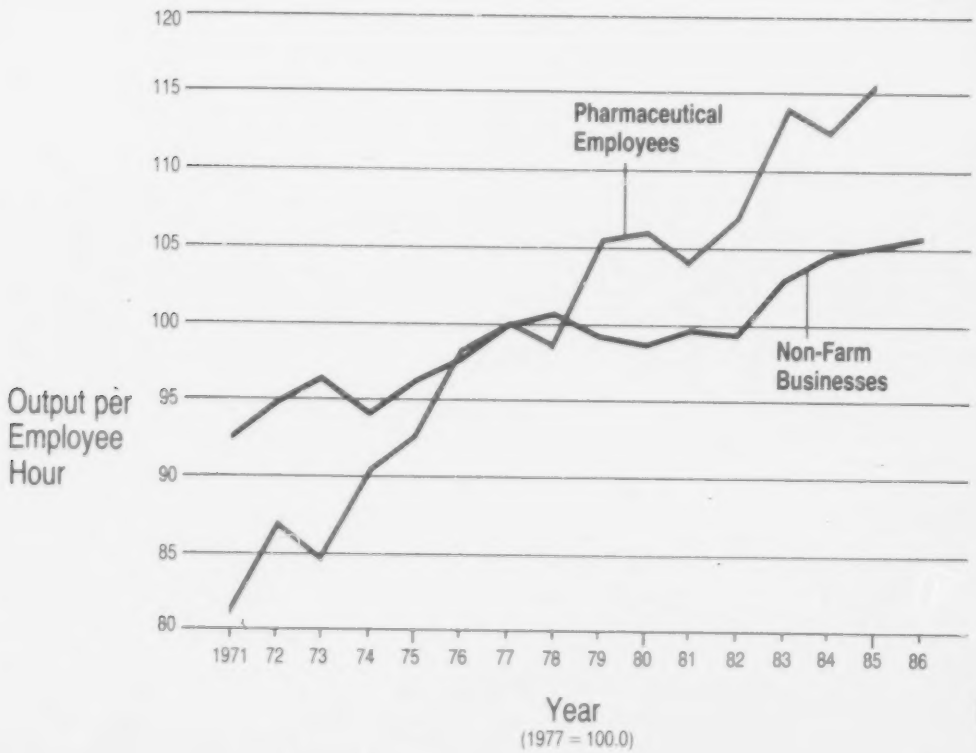
Productive Employees

The pharmaceutical industry's workforce is among the most productive of any industry. As measured by output-per-employee hour, the industry's employees (of whom one out of five work in R&D) increased productivity by 10 percent more than other businesses' employees in 1985.

Employee Productivity

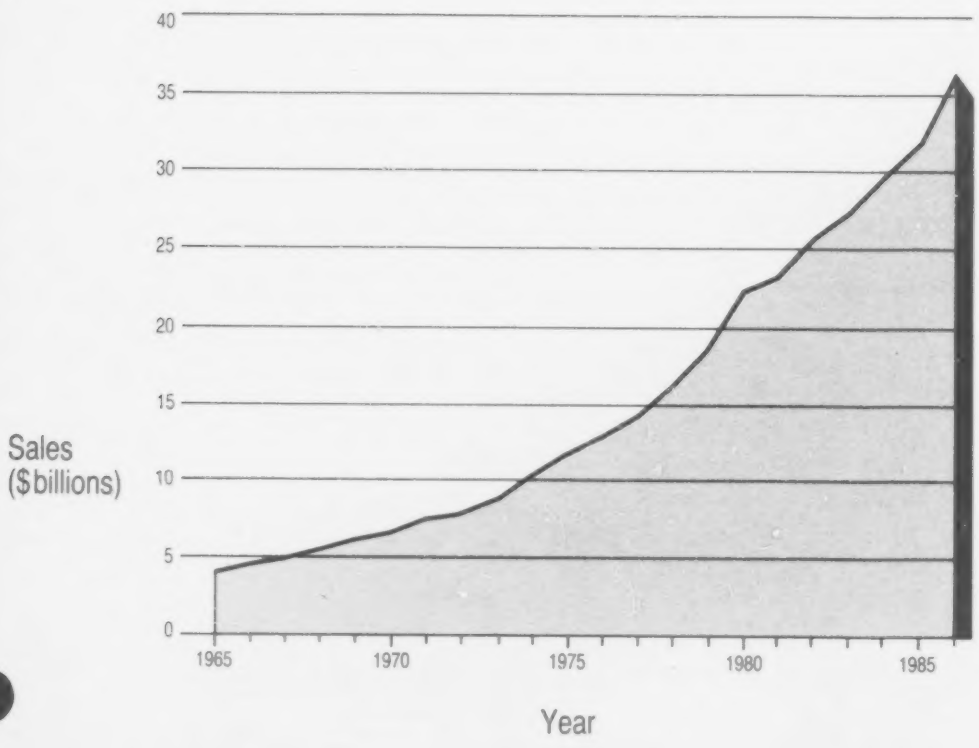


Source: Office of Publications, U.S. Bureau of Labor Statistics, U.S. Department of Labor, (various statistical series).

The Industry's Contribution As A Producer . . .

Total worldwide annual sales of PMA members grew from $4.1 billion in 1965 to $36.1 billion in 1986. While domestic annual sales increased 731 percent, foreign sales grew 1,014 percent for the same period. In 1986, foreign sales represented one-third of total worldwide sales, compared to one-quarter in 1965.

Worldwide Sales 1965–1986

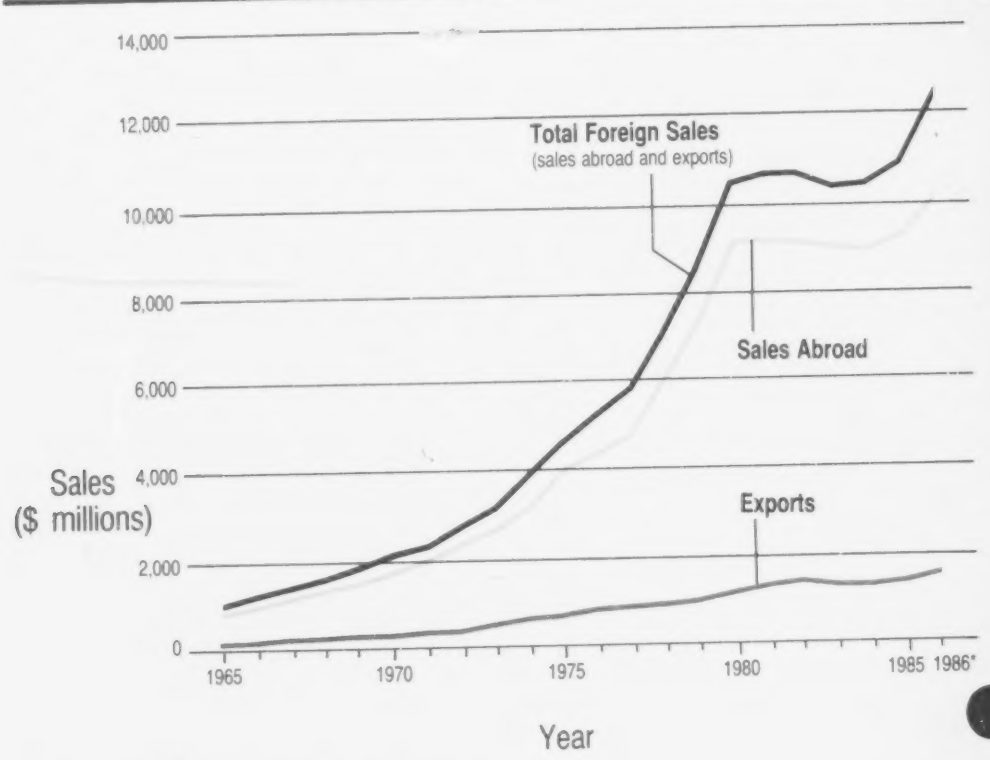


Source: PMA Annual Survey

A Multi-National Industry

The pharmaceutical industry is multi-national in scope. Many companies have subsidiaries or jointly-owned affiliates in other countries. Many others engage in international operations. Sales of PMA members achieved through manufacturing abroad greatly exceed direct exports from the U.S. In 1986, more than one-third of all sales were sales abroad.

Foreign Sales Of Ethical Pharmaceuticals By U.S.-Owned PMA Member Firms 1965–1986



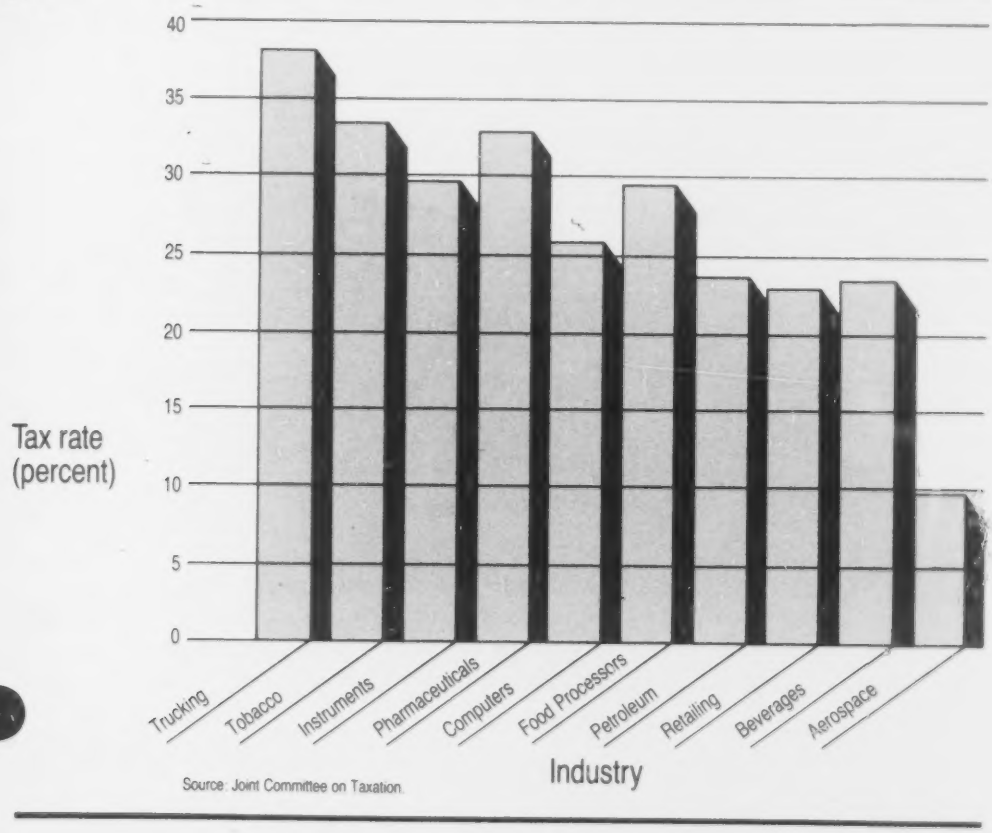
*Estimated.

Source: PMA Annual Survey, various years.

The Industry's Contribution As A Taxpayer . . .

The effective tax rate for the U.S. pharmaceutical industry is among the highest for all industries. Between 1980 and 1983, the average rate for the industry was 32.9 percent, the third highest.

Corporate Effective Tax Rates By Industry 1980–1983 Average

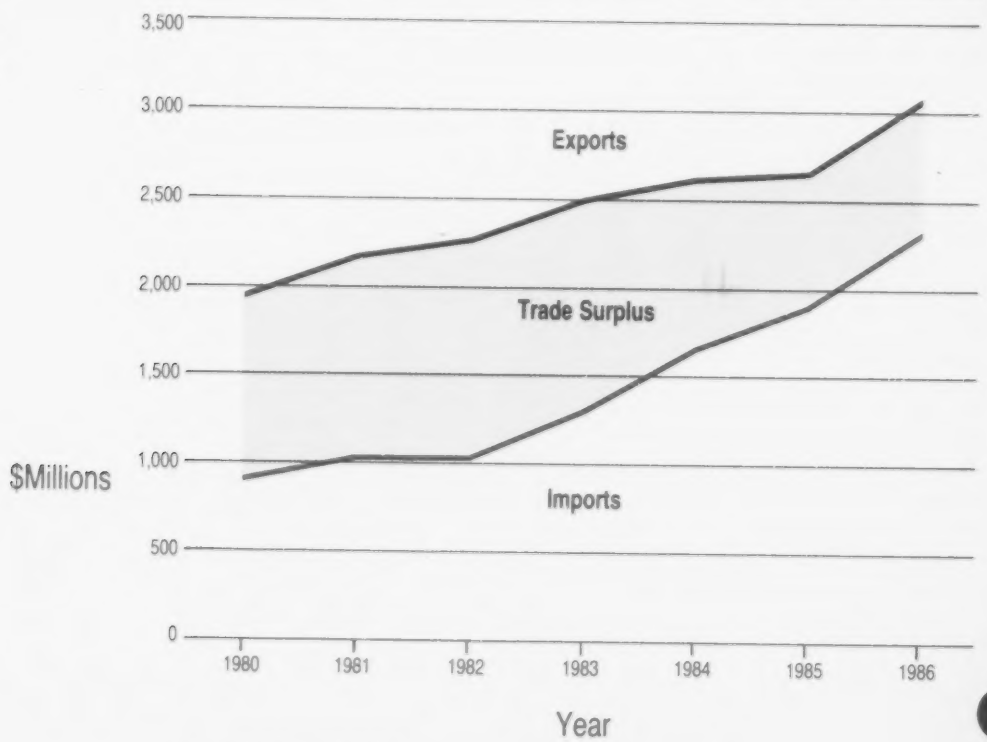


Source: Joint Committee on Taxation

The Industry's Contribution As A Trading Partner . . .

In a time of national concern about U.S. competitiveness and trade, the U.S. pharmaceutical industry is sustaining a favorable balance of trade. In 1986, the trade *surplus* from pharmaceuticals was $764 million.

Pharmaceutical Industry Trade Balance

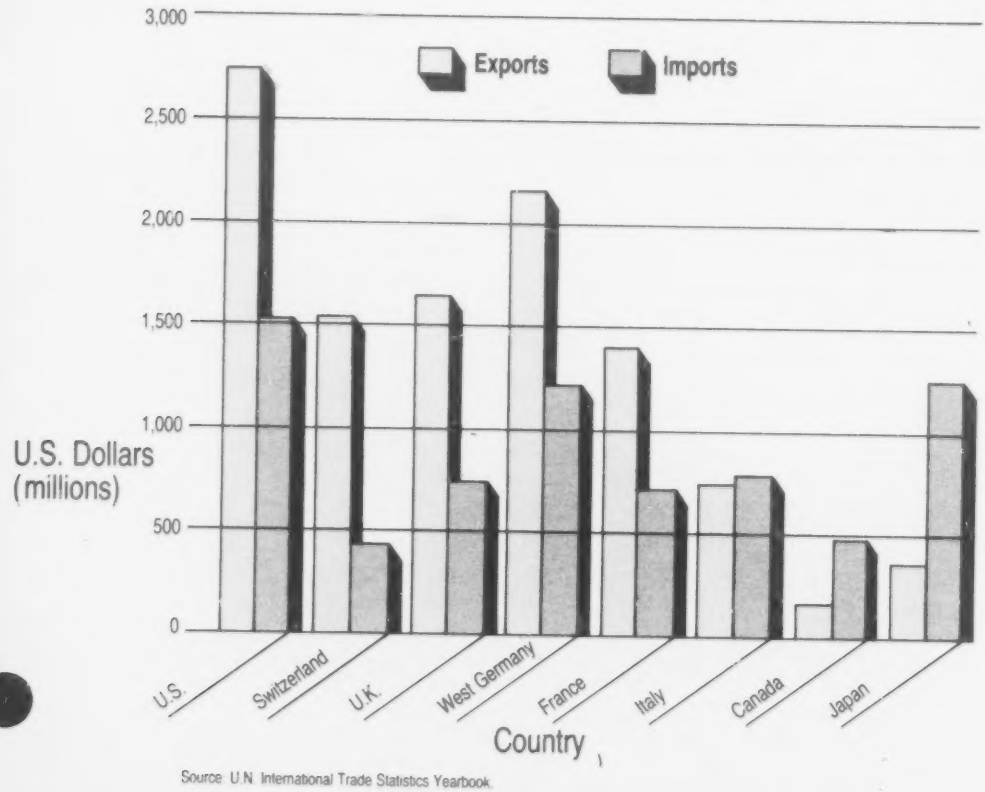


Note: Includes Biologicals; Medicinals and Botanicals; Finished Pharmaceutical Preparations.
Source: U.S. Department of Commerce.

The Leading Exporter And Importer

In 1984, the U.S. became both the leading exporter and importer of pharmaceuticals worldwide. The Federal Republic of Germany, which had been the leading exporter and importer in 1980, is now the second leading exporter. Japan is the second leading importer.

World Trade In Medicinal And Pharmaceutical Products, 1984

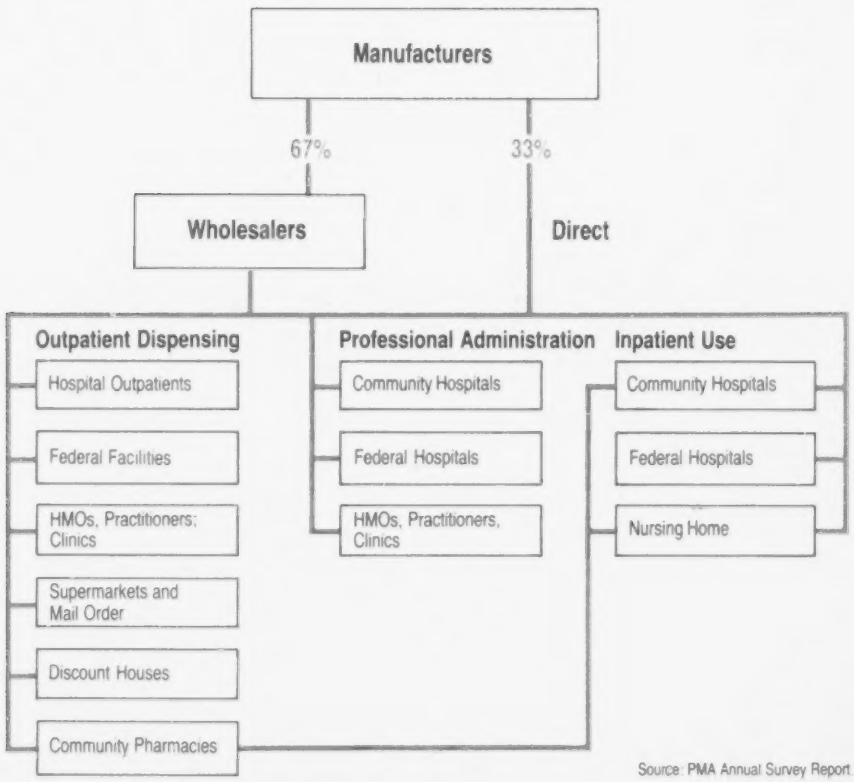


Source: U.N. International Trade Statistics Yearbook

The Industry's Contribution As A Distributor. . .

The pharmaceutical industry distributes its drug products to consumers through many channels. About 67 percent is distributed through wholesalers to hospitals, HMOs, and retail pharmacies. The remaining 33 percent is sold directly by manufacturers to these outlets.

Channels Of Prescription Drug Distribution

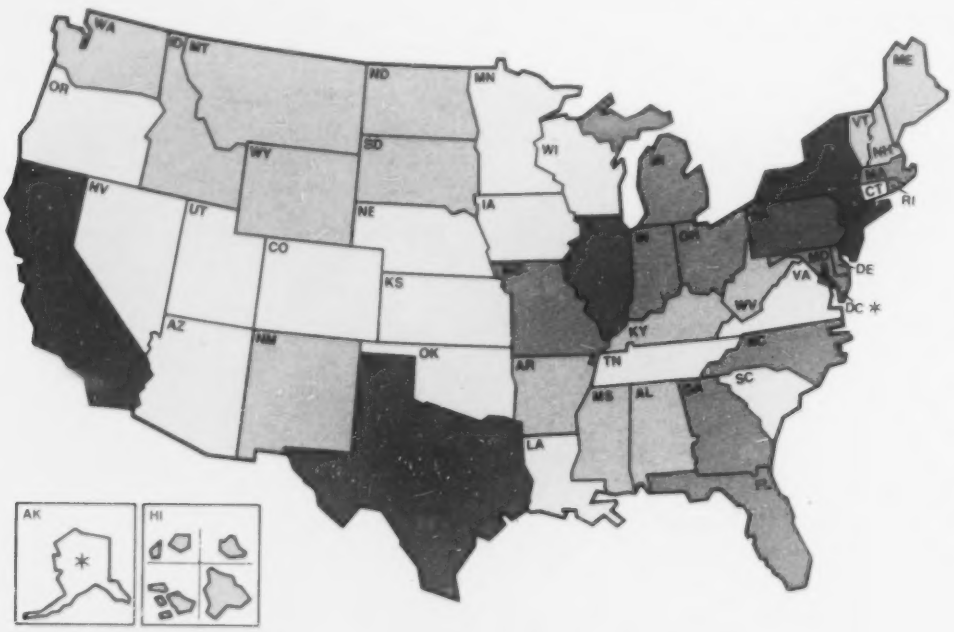


Source: PMA Annual Survey Report

Industry Facilities Throughout The United States

In the United States, drug industry facilities are located in every state but Alaska, with the concentration in New Jersey, New York, Pennsylvania, Indiana, Illinois, Michigan, Missouri, Ohio, California and Puerto Rico.

Locations For Industry Facilities In The U.S.



100 Facilities or more
50–99 Facilities
25–49 Facilities
10–24 Facilities
less than 10 Facilities
* No facilities

Source: U.S. Department of Commerce, Bureau of Census

II. The Industry's Commitment To Research And Development

The essential characteristic of the research-based pharmaceutical industry is its continued commitment to discovering, developing and marketing major new therapeutic medicines. This mission requires an increasing financial commitment—from $600 million in 1970 to $4.6 billion in 1986.

Innovation in new drug therapy has become significantly more complex, time-consuming and costly over the years. For example:

- It takes an average of 10 years from the time a drug is discovered until it is available to the patient.
- In 1986, the average FDA review time was 34.2 months, two months longer than that required for 1985 products.
- It costs well over $100 million to discover and develop a new drug product.
- Approximately 15 percent of U.S. pharmaceutical sales and export revenues was reinvested in research in 1986.

U.S. pharmaceutical companies discover, research and develop most new drug therapies.

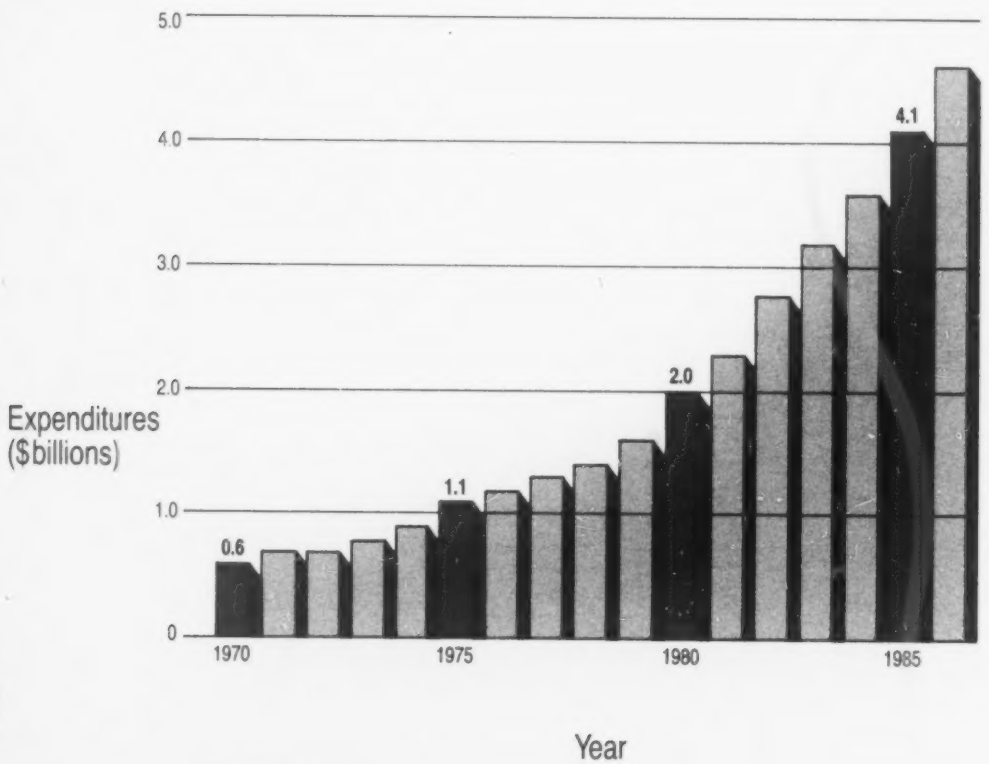
Over 90 percent of the most prescribed drugs in the U.S. was discovered by the research-based pharmaceutical industry.

In the last four decades, the industry has produced a wide range of therapeutic products. It has now turned to biotechnology and other new technologies to continue to pursue new avenues for drug innovation.

Major Research Commitment —R&D Expenditures

In 1986, the research-based pharmaceutical companies invested a record $4.6 billion in research and development, an increase of 12.2 percent from 1985. This research commitment has been growing at a rate of more than 10 percent a year. The industry's research investment has doubled every five years since 1970.

R&D Expenditures For PMA Member Firms

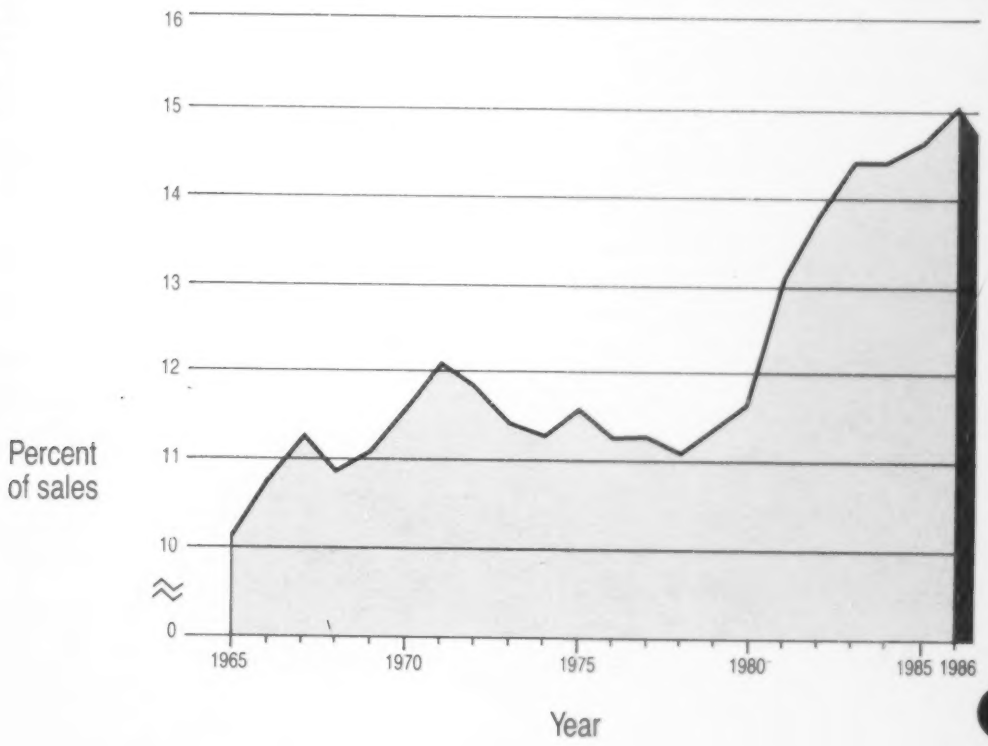


Source: PMA Annual Survey

Research Spending—A High Percentage Of Sales

In 1986, 15 percent of U.S. pharmaceutical sales and export revenues were reinvested in research —up from 11.3 percent ten years earlier. During the 1980s alone, the portion of sales revenues reinvested into R&D increased by more than 28.2 percent.

R&D Expenditures As A Percentage of Sales 1965–1986

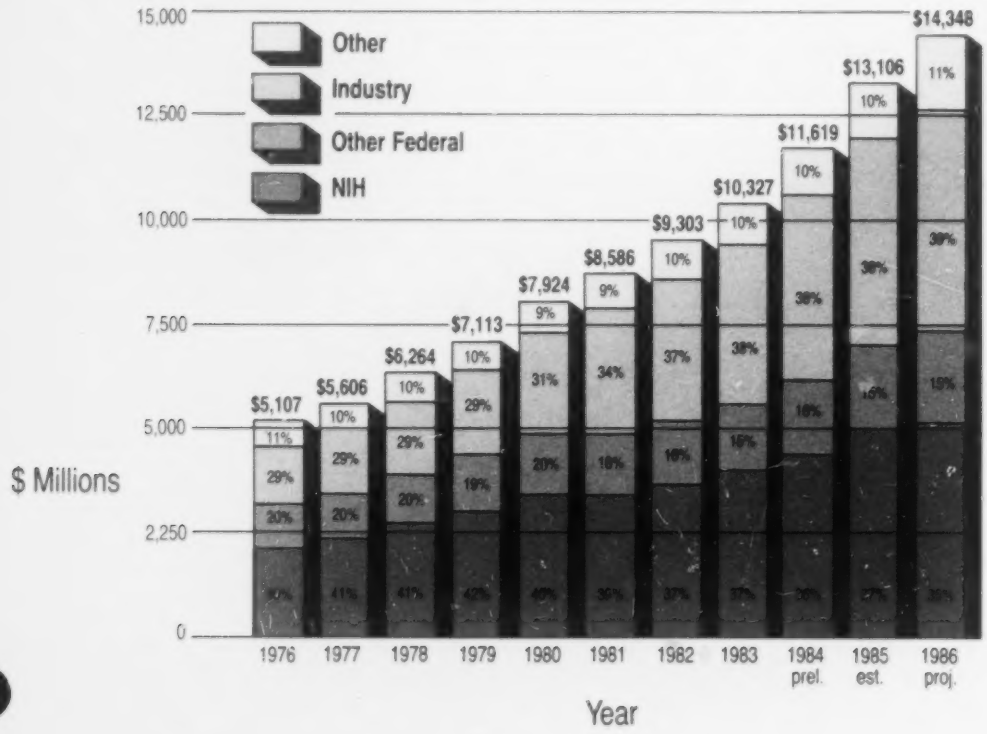


Source: PMA Annual Survey

A Major Source Of Medical Research

Private industry's investment in medical research and development now outstrips the amount committed by the National Institutes of Health. In 1986, 39 percent of total spending for biomedical R&D in the U.S. was invested by industry compared with 35 percent by the National Institutes of Health. The research-based pharmaceutical industry's investment of $4.6 billion in 1986 nearly matches the $5 billion appropriations for NIH health research. Pharmaceutical R&D investment will soon surpass the NIH.

National Support For Health R&D By Source, 1976–1986



Source: National Institutes of Health

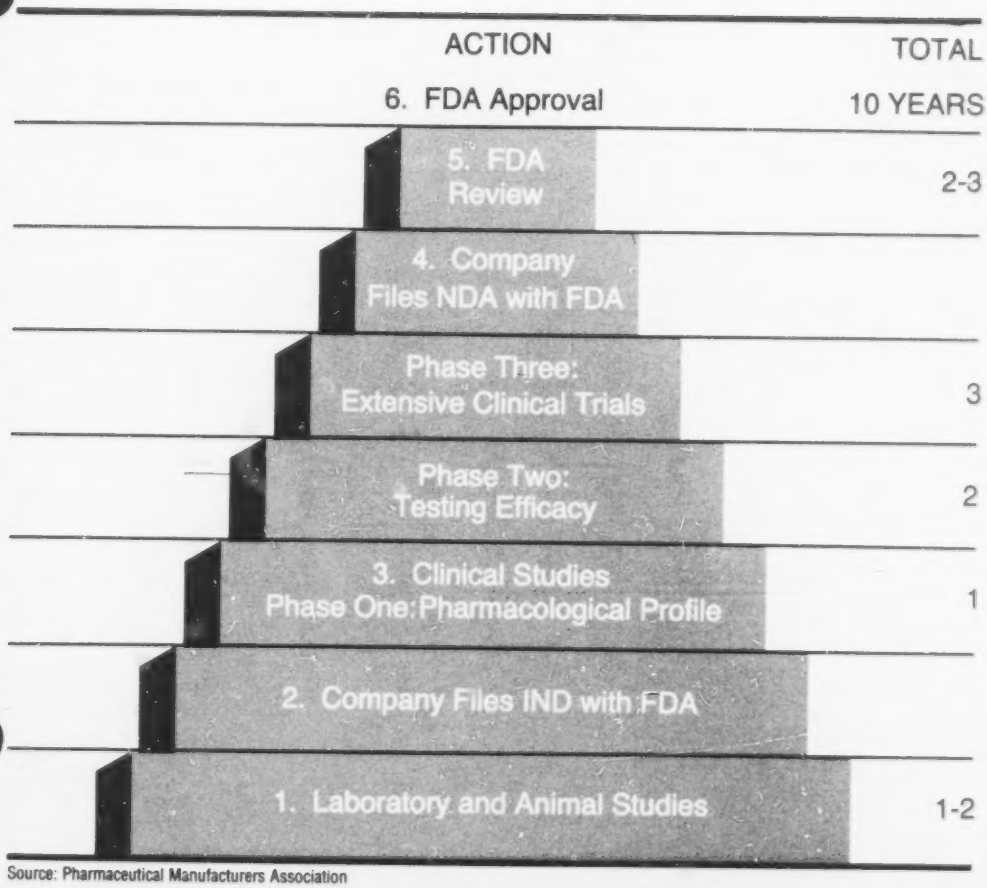
The High Cost Of Drug Development

On average, it costs well over $100 million to bring a new drug through discovery, clinical testing, development and FDA approval to begin marketing. This cost has increased sharply in recent years. Major contributors to the increased cost include the intricate nature of modern research and the expense of the highly sophisticated laboratory equipment it requires. In addition, as the focus of research has shifted toward chronic and degenerative diseases, complicated and extensive clinical testing is often necessary to prove efficacy of new medicines.

A Decade From Discovery To Marketing

It takes approximately one decade from the time that the new drug is discovered until it is available to the patient in a pharmacy or hospital.

The Steps Toward Drug Approval

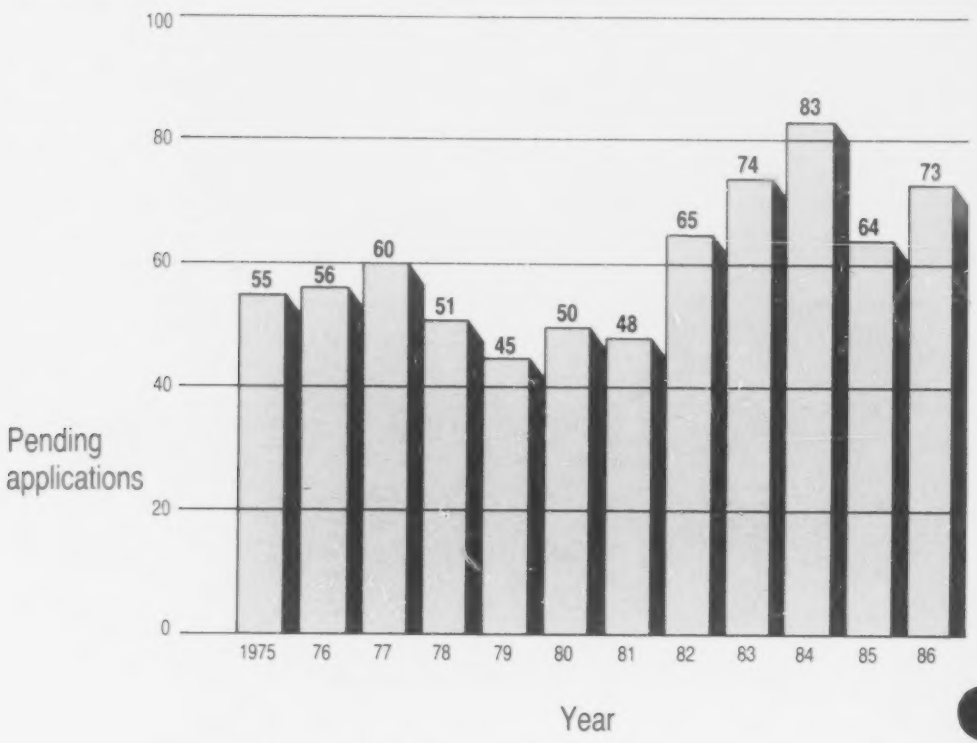


Source: Pharmaceutical Manufacturers Association

FDA Backlog On The Rise

FDA's workload and backlog for new drug applications has increased.

NME Backlog

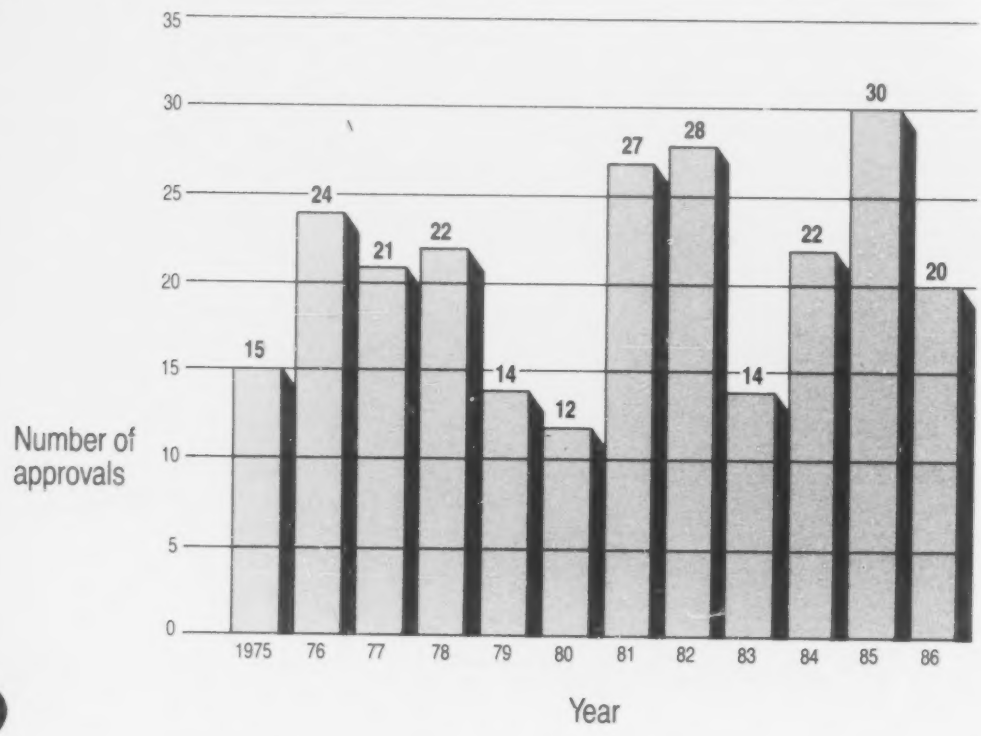


Source: U.S. Food and Drug Administration

FDA New Drug Approvals

The FDA approved 20 new drugs (new molecular entities or NMEs) in 1986, down from 30 approved in 1985 and 22 in 1984.

U.S. NME Approvals Per Year



Source: U.S. Food and Drug Administration.

New Drugs Approved In 1986

The 20 drugs approved by the FDA in 1986 include the following:

New Drugs & Biologicals Approved In 1986

NAME	MANUFACTURER	CATEGORY
	Drugs (New Molecular Entities)	
Alfenta	Janssen	Opioid analgesic for anesthesia
Atrovent	Boehringer Ingelheim	Bronchodilator
Azactam	Squibb	Antibiotic
Brevibloc	DuPont Critical Care	Beta-blocker
Buspar	Bristol-Myers	Anxiolytic
Cibacalcin	Ciba-Geigy	Hypocalcemic for Paget's disease
Cyclokapron	Kabivitrum	Hemorrhage prevention for hemophiliacs
Enkaid	Bristol-Myers	Anti-arrhythmic
Exirel	Pfizer	Bronchodilator
Lamprene	Ciba-Geigy	Anti-leprosy
Nix	Burroughs Wellcome	Pediculocide

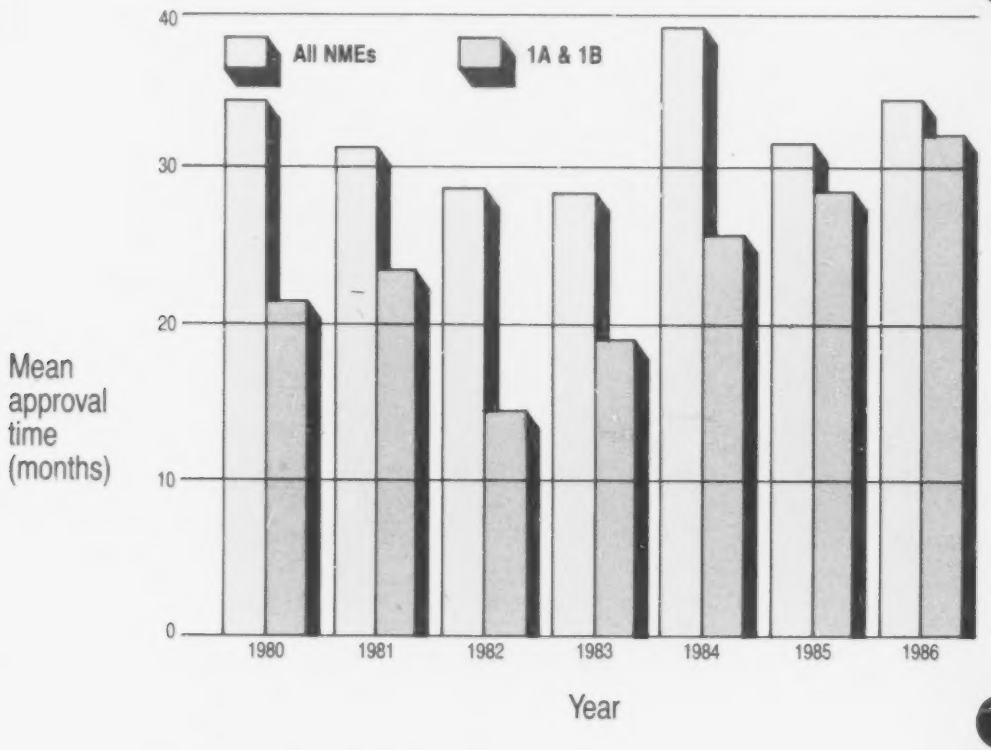
Source: U.S. Food and Drug Administration

NAME	MANUFACTURER	CATEGORY
Drugs (New Molecular Entities) (Continued)		
Noroxin	Merck	Antibacterial
Ocufen	Allergan	Intra-operative miosis
Orudis	Wyeth	NSAID (anti-arthritic)
Pepcid	Merck	H_2 antagonist (anti-ulcer)
Provocholine	Hoffmann-La Roche	Asthma diagnostic
Technescan HIDA	Merck	Imaging agent
Tegison	Hoffmann-La Roche	Antipsoriatic
Tenex	Robins	Antihypertensive
Unasyn	Pfizer	Anti-infective
Biotechnology Products (Biologicals)		
Intron A	Schering-Plough	Hairy cell leukemia
Orthoclone OKT3	Ortho	Kidney transplant rejection
Recombivax HB	Merck	Hepatitis B
Roferon-A	Hoffmann-La Roche	Hairy cell leukemia

A Long Review Process

The average FDA review time for the 20 new molecular entities approved in 1986 was 34 months, two months longer than that required for 1985 products. Shown below are mean review times since 1980 for all NMEs and for NMEs rated 1A and 1B ("fast track" drugs representing FDA assessments of therapeutic gains.)

Mean Approval Times 1980–1986

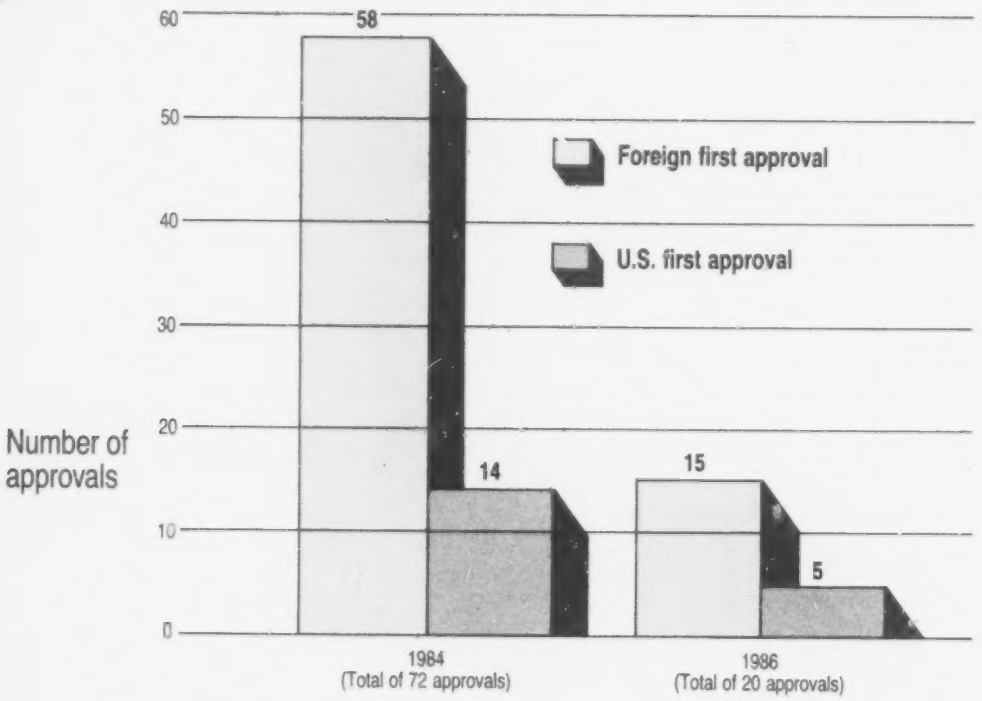


Source: U.S. Food and Drug Administration.

New Drugs Often Approved Overseas First

Of the 72 new molecular entities approved by the Food and Drug Administration between 1984 and 1986, 58 were first approved in a foreign country, a trend that has become common in recent years. It should be noted that companies often seek approval for their products first in foreign countries.

NMEs Marketed Abroad Prior To U.S. Approval (1984–1986)



Source: PMA Survey

FDA Approval Lags Behind Foreign Marketing

Over the past three years (1984-1986), more than half of the 58 drugs already approved abroad were available in at least four countries at the time of FDA approval. The average lag time between first foreign marketing and FDA approval for the 58 products was 6.3 years.

U.S. NME Approvals Country Of First Approval

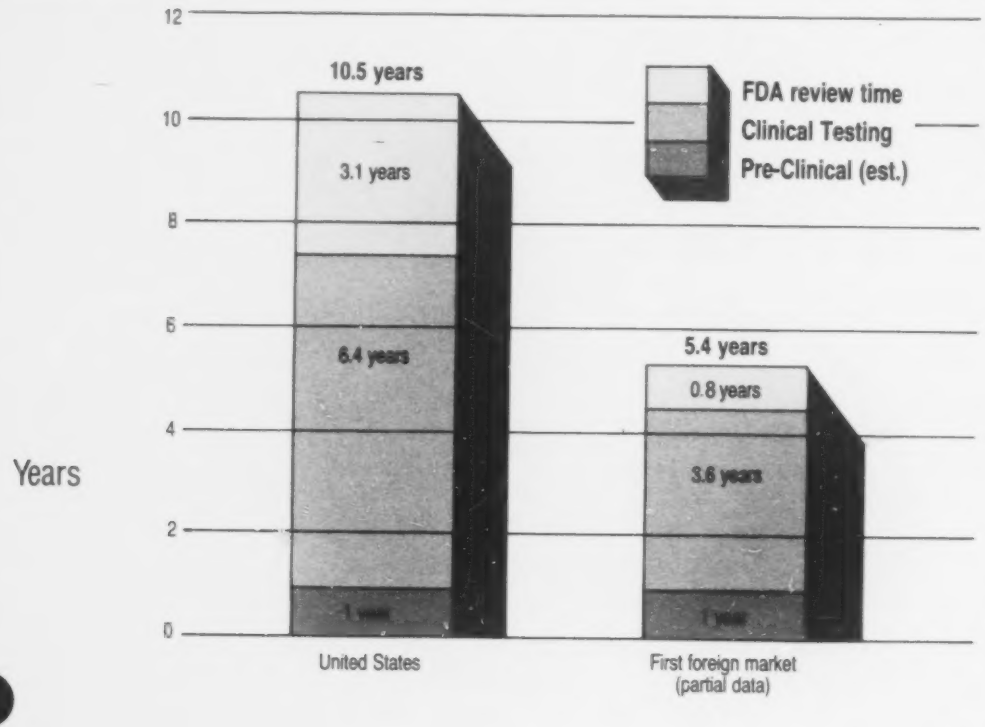
Total NMEs	58
Germany	43
United Kingdom	34
Switzerland	33
France	27
Italy	28
Japan	16
Canada	11
Sweden	9
Belgium	8
Netherlands	3

Source: PMA Survey

Average Drug Development Times Longer In The U.S. Than Abroad

For those 1986 products first approved overseas, the average review time was 0.8 year, compared with a mean review time of 37 months taken by the FDA for those same products. Average development times for these 15 products in the first foreign market and the U.S. are compared below.

Average Development Time 1986 NMEs First Approved Abroad



Source: PMA Survey

U.S. Companies Lead In Drug Discovery

Between 1940 and 1986, 1,178 drugs were introduced in the U.S. market. Nearly 62 percent was discovered in the U.S.

New Single Chemical Entity Drugs Introduced To U.S. Market 1940–1986, By Country Of Origin

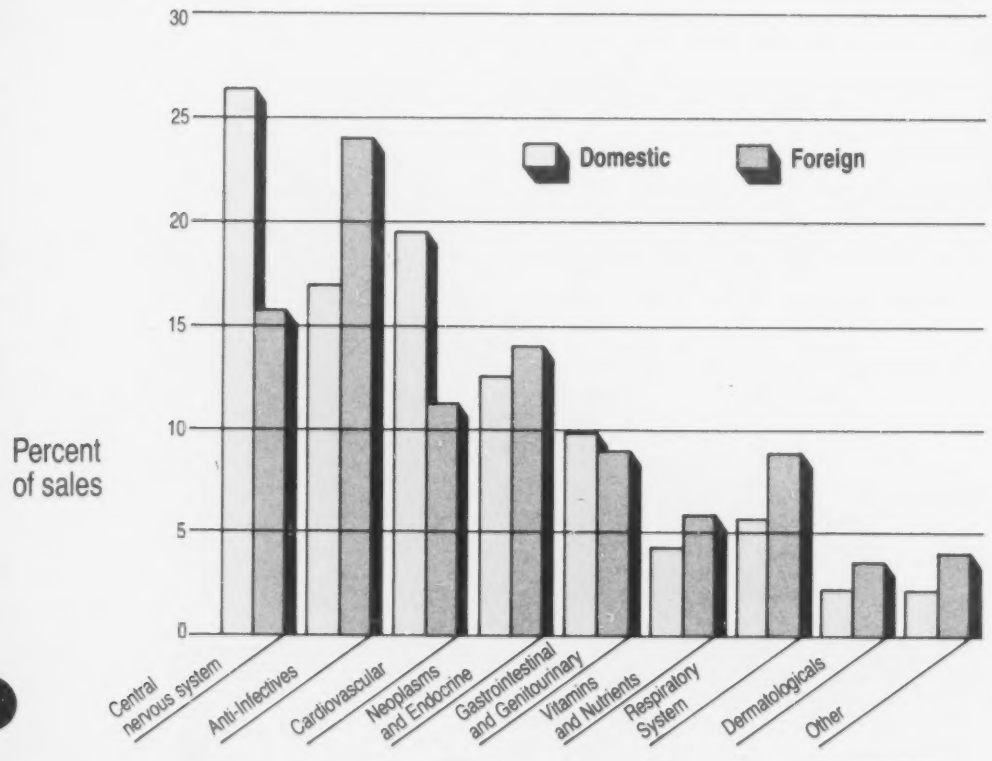
COUNTRY OF ORIGIN	PERCENTAGE OF TOTAL 1,178 NEW DRUGS
United States	61.6%
Switzerland	6.8%
United Kingdom	6.2%
West Germany	5.4%
France	3.3%
Japan	1.7%
Denmark	1.5%
Belgium	1.5%
Sweden	1.3%
Holland	1.3%
Italy	1.0%
Mexico	.8%
Austria	.3%
Canada	.3%
Australia	.2%
Hungary	.2%
Czechoslovakia	.1%
Argentina	.1%
India	.1%
Other	6.3%
TOTAL	100%

Source: PMA Analysis of Paul De Haen data

A Wide Range Of Therapies

The pharmaceutical industry produces drugs in many therapeutic categories. In the U.S., central nervous system products are the leading category. Abroad, anti-infectives are the leading sellers.

PMA Member Firms Domestic And Foreign Sales Of Ethical Drugs For Human Use

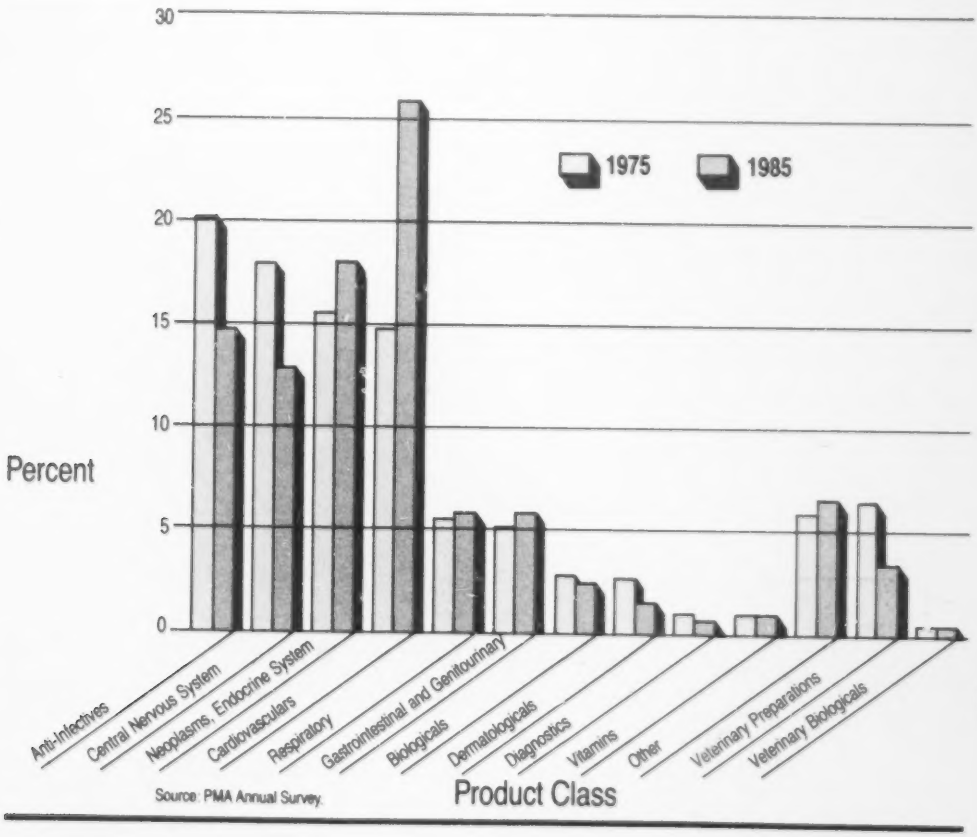


Source: PMA Annual Survey

Shift In The Types Of Drugs Being Developed

The focus of industry R&D has changed significantly in the last 10 years. In 1975, 20.1 percent of R&D went to anti-infectives while 14.9 percent was for cardiovascular products. In 1985, R&D for anti-infectives dropped to 14.9 percent while cardiovascular R&D rose to 25.8 percent.

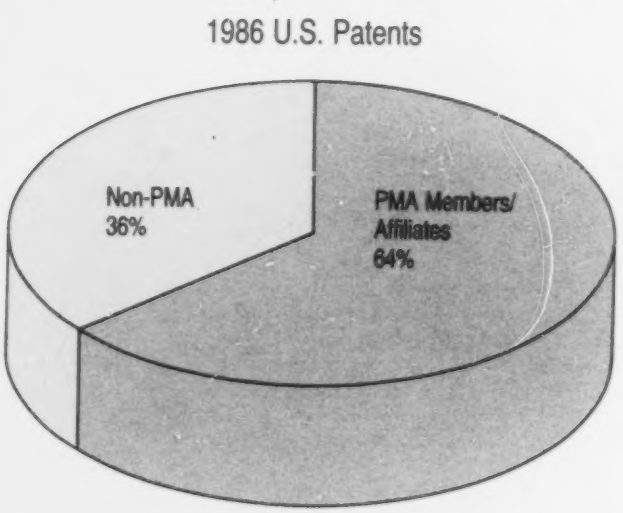
U.S. R&D, 1975 And 1985



The New Research Challenge: Biotechnology

Biotechnology is opening major new avenues for drug innovation. The U.S. Patent Office issued 1,232 biotechnology-related patents in 1986, of which more than half were pharmaceutical- or health-related. PMA members were issued 64 percent of the pharmaceutical- or health-related patents issued to U.S. corporations.

U.S. Corporate Pharmaceutical/ Health Care Biotechnology Patent Ownership



Source: OMEC International, Inc.

III. The Value Of Pharmaceuticals In Improving Health Care And In Reducing The Costs Of Illness

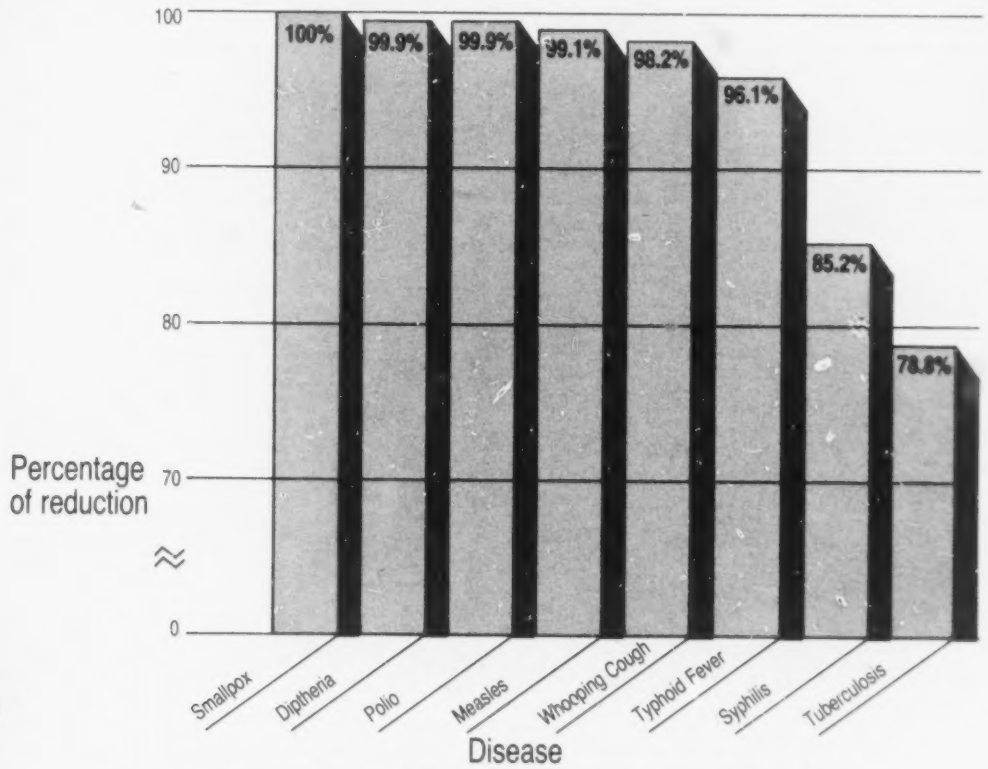
Among the most important technological advances of the Twentieth Century are those that have strengthened our ability to conquer disease and have extended the length and enhanced the quality of human life.

Medicines discovered and developed by the research-based pharmaceutical industry have yielded dividends in both lives and dollars saved.

Medicines have contributed significantly to the reduction of disease. Medicines have virtually eliminated diphtheria and polio.

Improved Health: Reduced Morbidity

Reduction In Reported U.S. Cases Of Selected Diseases 1940–1985

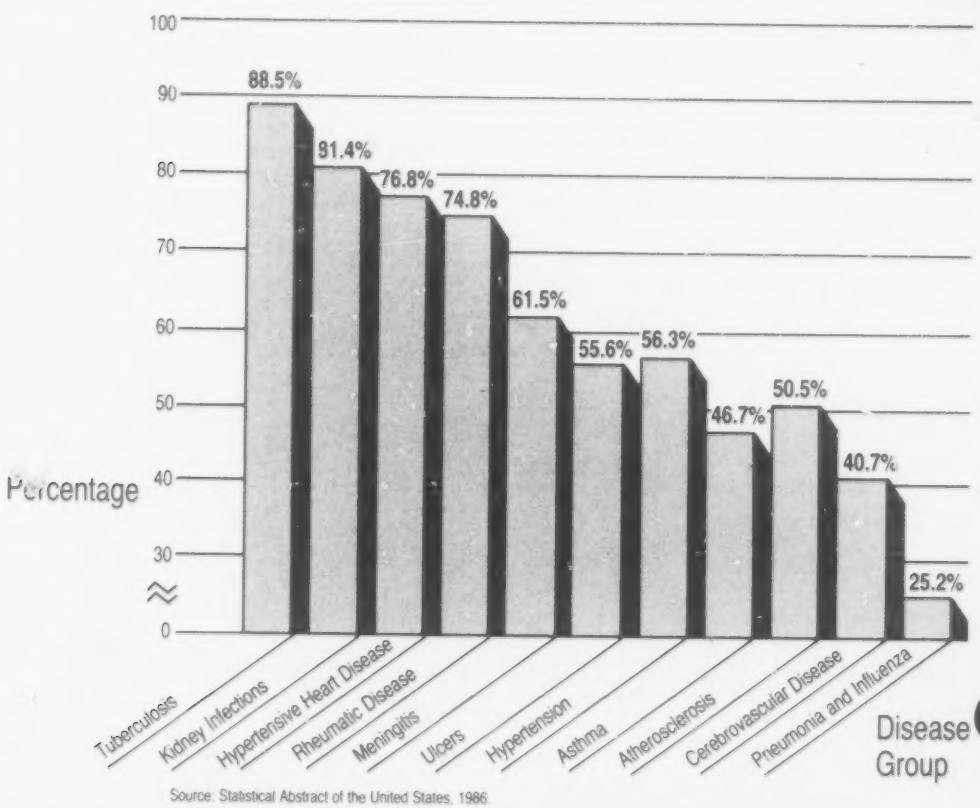


Source: Morbidity and Mortality Weekly Report, Annual Summary, 1984, U.S. Dept. of Health and Human Services

Improved Health: Reduced Mortality

Pharmaceuticals have helped reduce deaths from diseases such as tuberculosis, kidney infection and hypertensive heart disease.

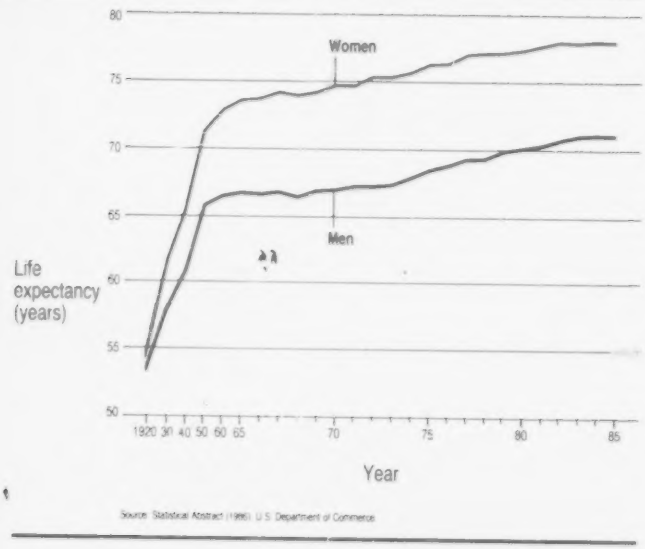
Mortality: Reduction In U.S. Deaths Per 100,000 Population From Selected Diseases 1960–1985



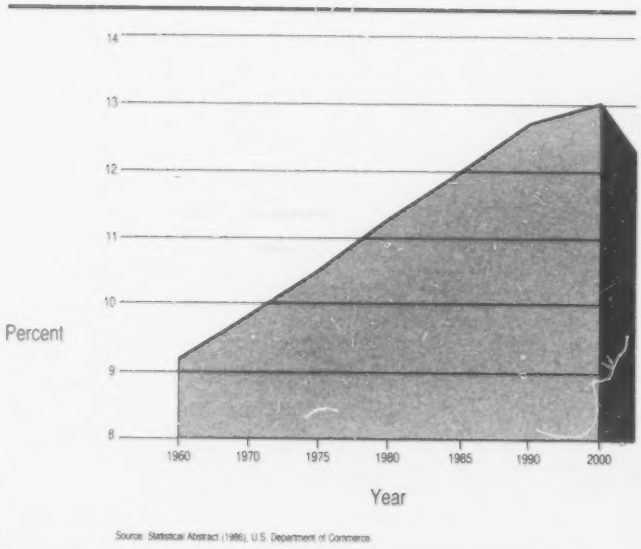
Source: Statistical Abstract of the United States, 1986

Improved Health: Increased Life Expectancy

New medicines have helped increase life expectancy. The average life expectancy for a person born in 1920 was 54.1 years, compared to 74.7 years today. The percent of people 65 years and older is increasing dramatically and will continue to do so through the end of the century.



U.S. Expectation Of Life At Birth 1920–1985



Over-65 Population As A Percent Of U.S. Population 1960–2000

Economic Benefits

Drugs not only reduce sickness and save lives, they also save money. They usually represent the least expensive form of health care. For example:

- Use of beta-blockers to prevent second heart attacks may save $1.6 billion to $3 billion per year.
- Medicaid expenditures for patients using an anti-ulcer drug have been shown to be about 70 percent less than for patients not using the drug.
- The use of antibiotics to prevent urinary tract infections reduces costs 33 percent per patient.
- For people with mild to moderate heart disease, the savings of using drugs over coronary bypass surgery is estimated at $500 million a year.
- Beta-blockers have saved as much as $1 billion annually when compared to the surgical alternative.

IV. Today's Health Care Environment

The changing health care environment greatly affects the research-based pharmaceutical industry.

Today's health care system has to deal with a different population—an older one—due in part to advances made by the pharmaceutical industry.

As a result of the growing population, inflation, and spiraling costs, national health expenditures continue to rise. So do per capita health care expenditures and health expenditures as a percentage of the GNP. By contrast, drugs as a percent of national health expenditures have steadily declined.

As cost-containment strategies are initiated it is important to remember that drugs represent a small percentage of national and Medicaid expenditures and can help to reduce the total costs of health care.

Health Care Labor Force

The number of people employed in the health care industry has grown from 4.2 million in 1970 to 7.9 million in 1984, an increase of more than 85 percent. Registered nurses form the largest health occupation group (1.4 million workers) followed by nursing aides (1.2 million).

U.S. Health Industry Personnel, Selected Categories

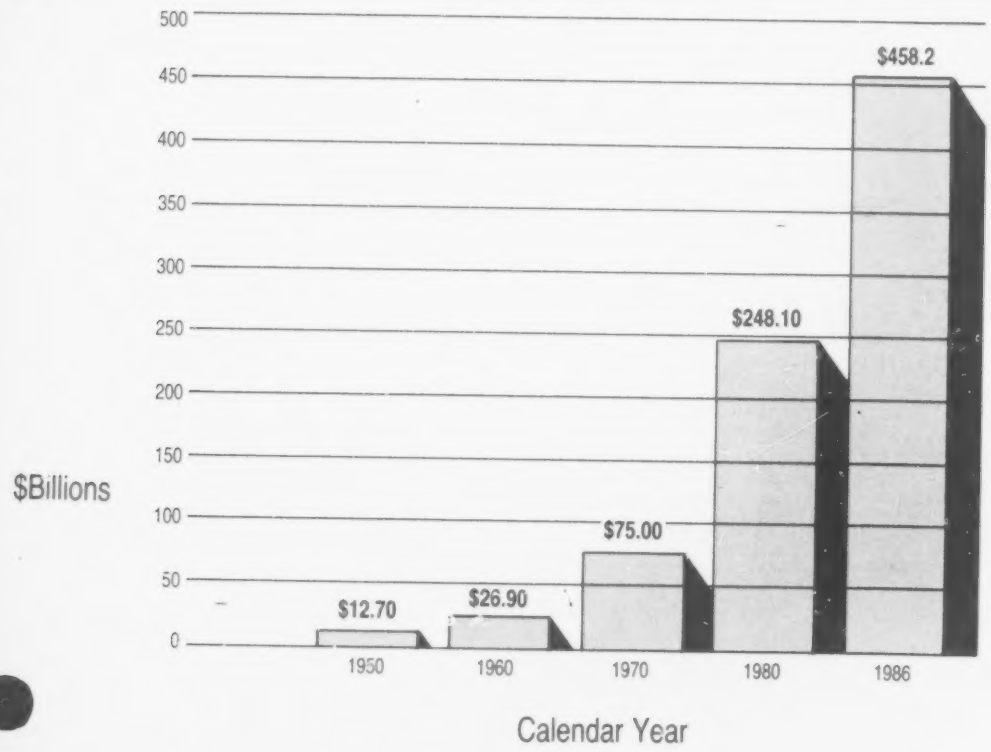
OCCUPATION	PERSONNEL
Doctors of Medicine	504,000 (a)
Doctors of Osteopathy	21,000 (a)
Dentists	163,000 (a)
Pharmacists	158,000 (a)
Health Technologists and Technicians	1,112,000 (b)
Optometrists	18,000 (a)
Physician Assistants	43,000 (b)
Registered Nurses	1,402,000 (b)
Practical Nurses	416,000 (b)
Nursing Aides	1,235,000 (b)
Managers, Medicine and Health	96,000 (b)

Source: (a) Business Mailers, 1986 data and (b) *1986 Statistical Abstract of U.S.*, 1984 data

National health expenditures have been doubling or tripling every decade.

National Health Expenditures On The Rise

National Health Expenditures (Current Dollars)

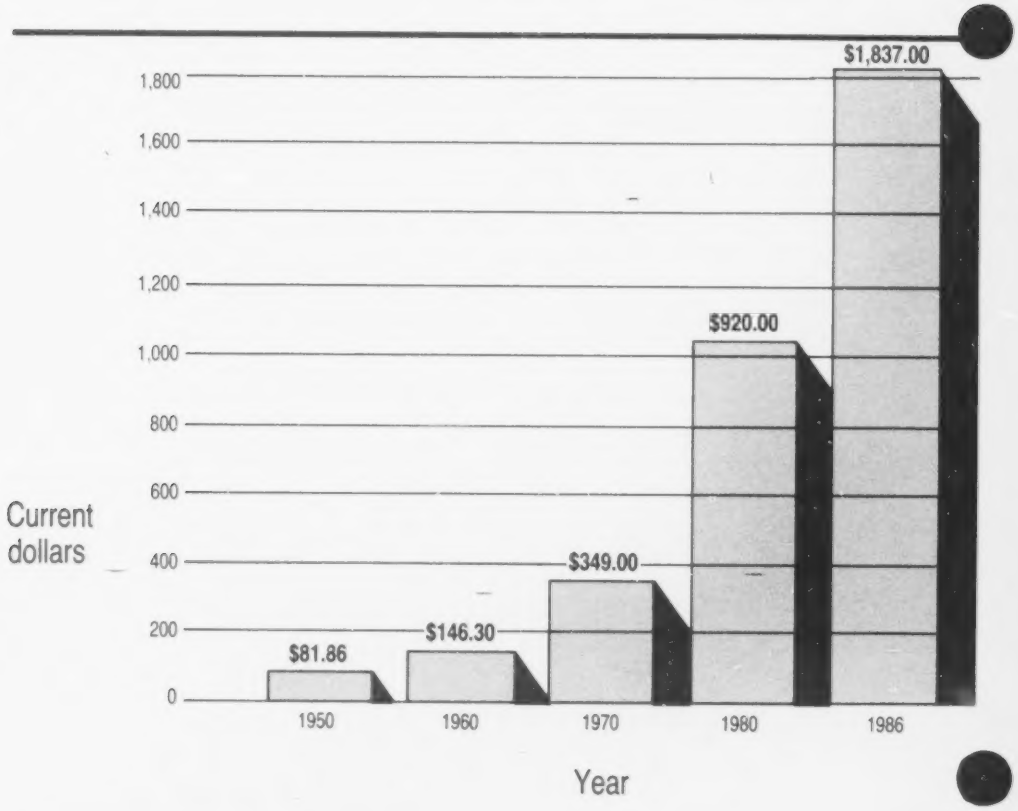


Source: Health Care Financing Administration

Per Person Expenditures On The Rise

Average per person health care expenditures have also been increasing steadily.

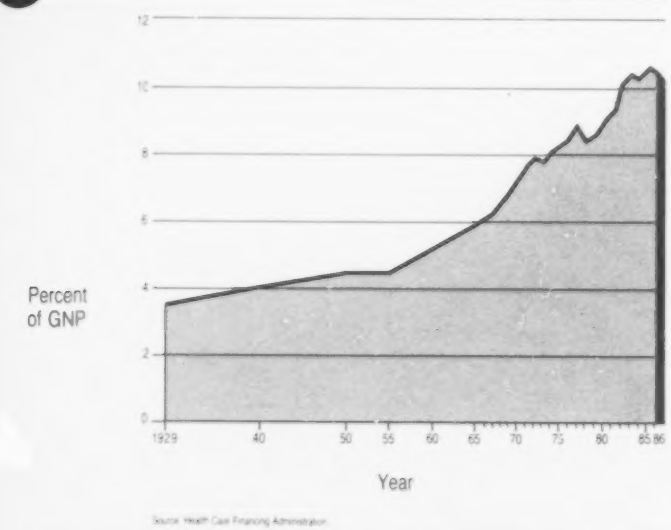
Per Capita National Health Expenditures



Source: Health Care Financing Review

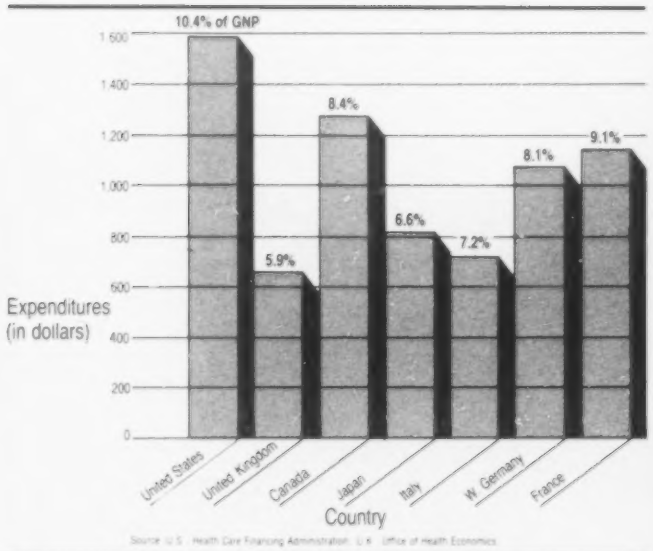
More of the nation's GNP is going to health care. The U.S. is the world leader in per capita spending and percent of GNP spent for health.

Health Expenditures As Percent Of GNP On The Rise



Source: Health Care Financing Administration

National Health Expenditures As Percent Of GNP Calendar Years 1929 – 1986



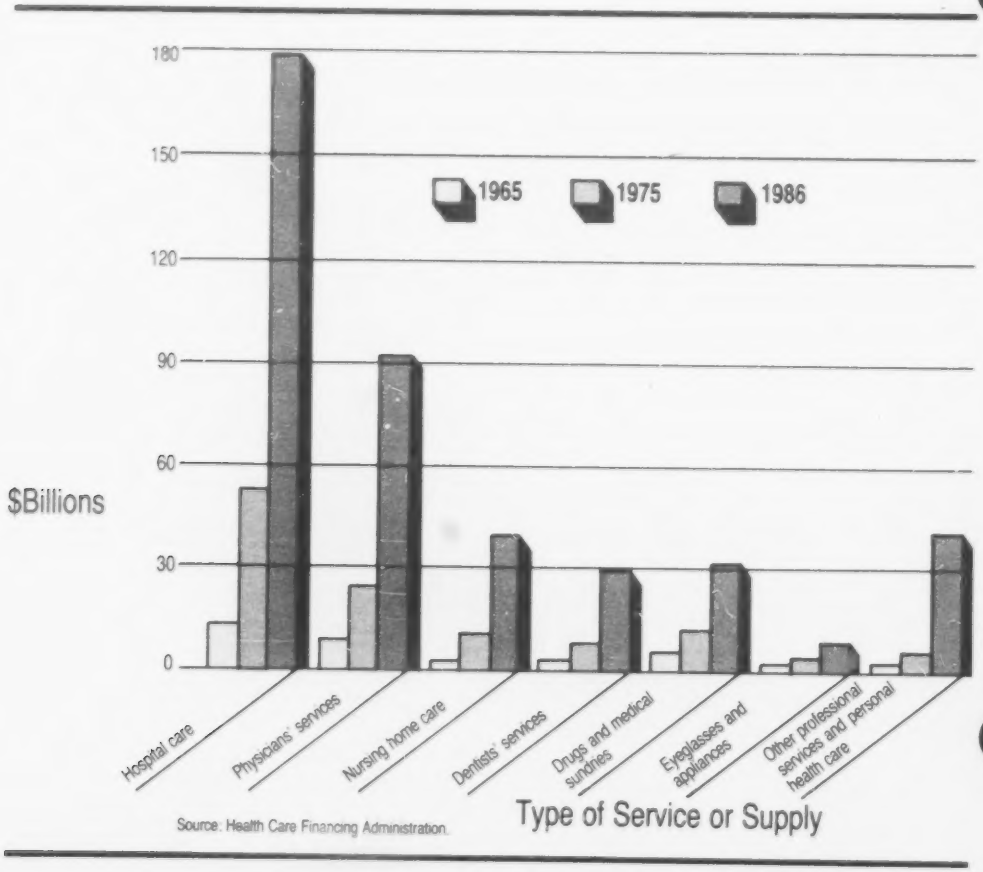
Source: U.S. Health Care Financing Administration; U.K. Office of Health Economics

International Comparisons Of Per Capita Health Expenditures 1984

The Breakdown Of Health Care Expenditures

Hospital care represents the largest proportion of expenditures and in 1986 accounted for 39.2 percent of all health costs. The next largest component was for physicians (20.1 percent).

Personal Health Care Expenditures

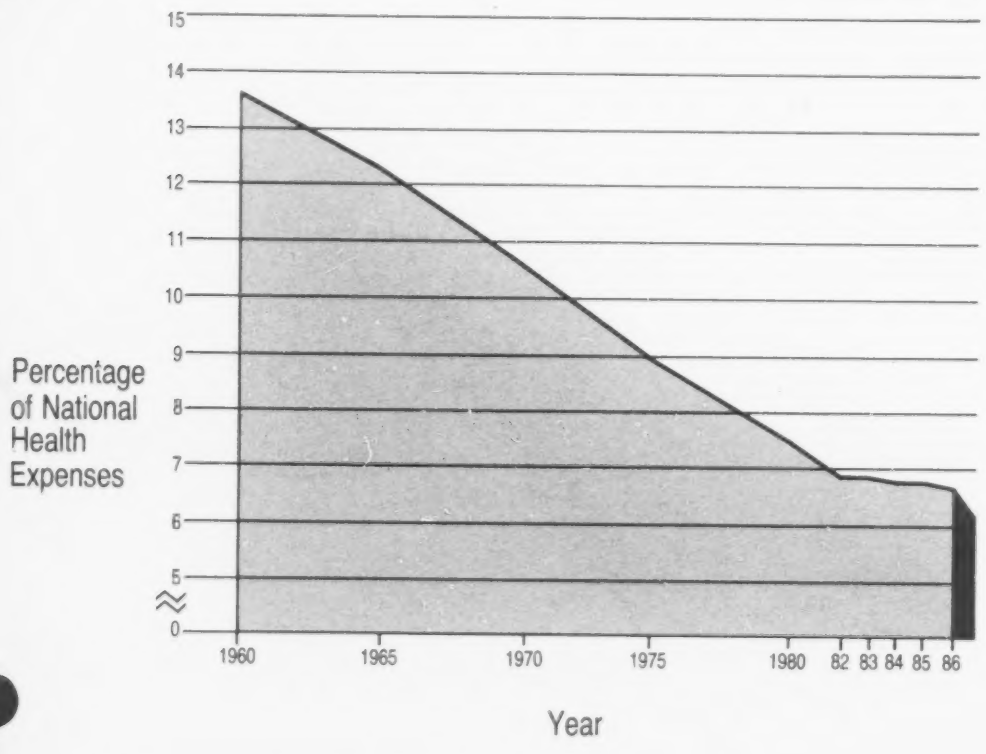


Source: Health Care Financing Administration.

Drugs As Percent Of National Health Expenditures On The Decline

Of every dollar spent on health care, less than seven cents is spent on drugs and sundries. That figure has declined steadily—down from 13.6 cents in 1960—despite the fact that drugs have displaced other more expensive forms of therapy.

Drugs As A Percentage of National Health Care Expenditures (Selected Calendar Years)

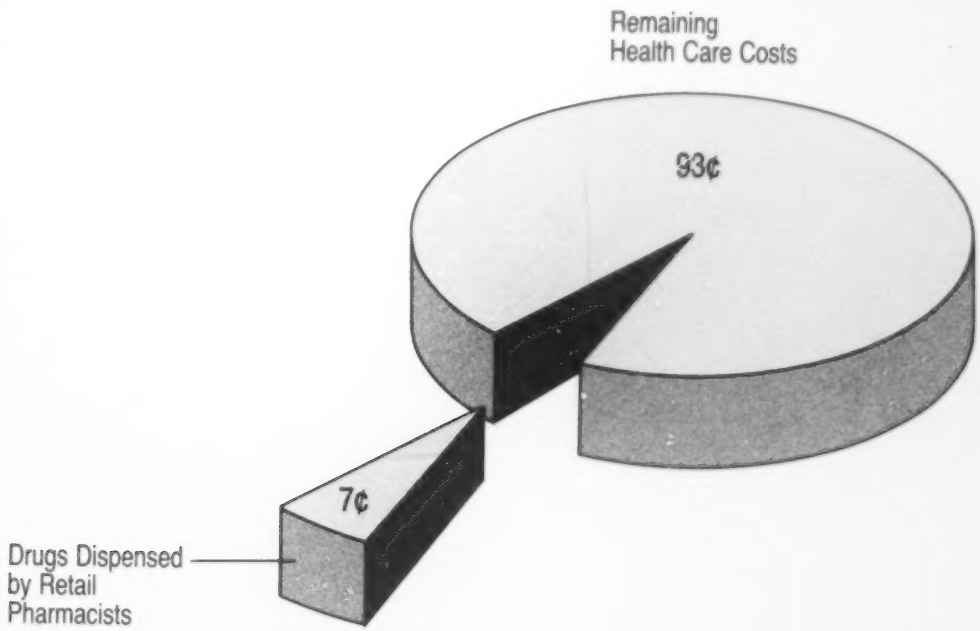


Source: Health Care Financing Administration

Percent of Medicaid Expenditures For Drugs

In 1986, less than seven cents of every Medicaid dollar was spent on prescription drugs dispensed by retail pharmacists.

The Medicaid Dollar



Source: Health Care Financing Administration.

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CHAPTER I

THE PHARMACEUTICAL INDUSTRY IN THE U.S.

BACKGROUND ON THE INDUSTRY

Although U.S. pharmaceutical manufacturing dates back to the mid-nineteenth century, it began to emerge as a major industry about 40 years ago. Prior to the 1930s there were many small firms, but only a few conducted research. Most pharmaceutical preparations were compounded by pharmacists in their shops and dispensed directly to consumers.

Introduction of the first sulfa drug in 1935 stimulated interest in pharmaceutical research and set the stage for the successful development of penicillin, the most significant of many pharmaceuticals developed during World War II. Sulfa drugs and antibiotics saved the lives of countless Americans and allies during that period. The 15 years between 1938 and 1953 have come to be known as "The Age of Antibiotics" because a number of useful new anti-infectives were discovered. Leadership in the industry, in total sales as well as in new drug discoveries, shifted from Europe to the U.S. during World War II. American firms substantially increased their research and development efforts.

This strong commitment to drug research and development is demonstrated by continued U.S. leadership in the introduction of new chemical entities during the past 40 years. A detailed discussion of these new product introductions is presented in Chapter II.

Numerous laws govern the production, distribution, and marketing of prescription drugs on both the state and federal levels. Federal regulation began with the 1906 Pure Food and Drugs Act. This act was designed to protect consumers by requiring, in part, that the ingredients of a medicine be truthfully stated on the package label. This law was strengthened considerably in 1938 with the passage of the Food, Drug and Cosmetic Act, under which drug manufacturers were required to demonstrate that a drug was safe for the use stipulated on the label. Federal control over prescription drugs was broadened further by the 1962 Amendments to the Food, Drug and Cosmetic Act which required manufacturers to show that a new drug is effective for its intended uses.

INDUSTRY OVERVIEW

Marketing research data for 1986 indicate that approximately 680 corporations and companies in the U.S. are engaged in the manufacture and sale of ethical and proprietary pharmaceuticals.[1] The U.S. Department of Commerce estimated that the value of shipments of pharmaceutical products by all manufacturers was $23.2 billion in 1985. PMA member firms traditionally account for more than 90 percent of the industry's U.S. sales of human dosage form drugs.

Many prescription drug firms produce other health-related products. In addition to prescription and over-the-counter drugs, many large firms also make veterinary products and agricultural chemicals. A large number of companies also manufacture medical equipment, medical devices, diagnostic products, and hospital supplies. Some firms are important suppliers of chemicals used in other industries.

Drug manufacturing facilities are concentrated largely in New Jersey, New York, Pennsylvania, Indiana, Illinois, Michigan, Missouri, Ohio, California, and Puerto Rico. Through networks of distribution centers and wholesale distributors, pharmaceutical products are available to patients in more than 6,800 hospitals and 65,000 pharmacies.

SALES AND SALES GROWTH

For the period 1965-1986, total worldwide annual sales of PMA member firms grew by nearly 800 percent, from $4.1 billion to $36.1 billion (Table 1-1). Until recently, the major source of this growth was increased foreign sales. Annual domestic sales increased 700 percent, but foreign sales increased by more than 1,000 percent. In 1980, foreign sales represented 47 percent of total worldwide sales, compared to 27 percent in 1965. However, this percentage declined to 34 percent by 1985.

SALES BY PRODUCT CLASS

As sales have grown over the years, the percentage of total sales has changed for various classes of products. In 1985, sales in the U.S. of drugs acting on the central nervous system led all other categories. In addition, the relative share for cardiovascular drugs more than doubled from 1972 to 1985 (Table 1-2).

---

[1] Based on data from IMS, America Ltd.

TABLE 1-1

U.S. AND FOREIGN PHARMACEUTICAL SALES
PMA MEMBER FIRMS
1965-1986
($ millions)

Year	Domestic Sales			Foreign Sales (including Exports)			Total Domestic and Foreign
	Human	Veterinary	Total	Human	Veterinary	Total	
1986*	$22,681.9	$994.5	$23,676.4	$11,541.4	$846.2	$12,387.6	$36,064.0
1985	20,265.0	888.5	21,153.5	10,129.6	742.7	10,872.3	32,025.8
1984	18,520.5	882.6	19,403.1	9,696.7	754.2	10,450.9	29,854.0
1983	16,218.2	876.8	17,095.0	9,645.4	765.8	10,411.2	27,506.2
1982	14,156.5	830.4	14,986.9	9,902.1	765.3	10,667.4	25,654.3
1981	12,100.4	761.6	12,872.0	9,895.2	763.1	10,658.3	23,530.3
1980	11,299.8	697.8	11,997.6	9,758.2	757.2	10,515.4	22,513.0
1979	9,558.8	644.2	10,203.0	7,916.2	648.6	8,564.8	18,767.8
1978	8,678.6	506.8	9,185.4	6,566.5	524.5	7,091.0	16,276.4
1977	7,907.1	428.6	8,335.7	5,403.8	406.7	5,810.5	14,146.2
1976	7,314.7	411.5	7,726.2	4,908.2	385.5	5,293.7	13,019.9
1975	6,602.8	301.0	6,903.8	4,467.6	328.7	4,796.3	11,700.1
1974	5,846.5	280.2	6,126.7	3,683.6	256.6	3,940.2	10,066.9
1973	5,258.6	269.1	5,527.7	3,078.5	199.5	3,278.0	8,805.7
1972	4,815.2	238.8	5,054.0	2,602.9	203.4	2,806.3	7,860.3
1971	4,510.4	199.0	4,709.4	2,212.7	175.2	2,387.9	7,097.3
1970	4,185.3	256.5	4,441.8	1,981.2	170.6	2,151.8	6,593.6
1969	3,894.8	216.4	4,111.2	1,702.3	154.5	1,856.8	5,968.0
1968	3,588.8	204.9	3,793.7	1,493.9	156.8	1,650.7	5,444.4
1967	3,199.1	211.8	3,410.9	1,350.8	147.2	1,498.0	4,908.9
1966	2,996.8	206.6	3,203.4	1,161.7	113.9	1,275.6	4,479.0
1965	2,773.1	180.7	2,953.8	998.5	99.2	1,097.7	4,051.5

*Estimated
Source: PMA Annual Survey.

Foreign sales of U.S. companies by product class, show different rankings than domestic sales with anti-infectives leading in sales in 1985 (Table 1-3).

TABLE 1-2

MANUFACTURERS' DOMESTIC SALES OF ETHICAL DRUGS FOR HUMAN USE
BY PRODUCT CLASS
1972*, 1981, 1982, 1983 and 1985

	Relative Share of Sales				
	1972	1981	1982	1983	1985
Central Nervous System	26.0%	25.4%	25.2%	26.2%	26.4%
Anti-Infectives	12.8	16.8	17.0	17.4	16.9
Gastrointestinal & Genitourinary	10.[illegible]	8.9	8.9	9.1	9.9
Neoplasms and Endocrine	12.0	13.6	13.5	13.3	12.5
Vitamins and Nutrients	7.6	8.8	8.3	5.6	4.2
Cardiovasculars	8.4	16.2	17.0	17.0	19.6
Respiratory System	6.6	5.7	5.2	5.9	5.7
Dermatologicals	3.3	3.2	2.8	2.6	2.4
Other	12.6	1.4	2.1	2.9	2.4
TOTALS	100.0%	100.0%	100.0%	100.0%	100.0%

* 1972 was the first year that data were reported consistently by product class.
Source: PMA Annual Survey.

TABLE 1-3

FOREIGN SALES OF ETHICAL DRUGS FOR HUMAN USE
BY PRODUCT CLASS AND DOSAGE FORM
1982-1985

	Relative Share of Sales		
	1982	1983	1985
Anti-Infectives	22.3%	21.3%	24.0%
Central Nervous System	16.2	15.4	15.9
Neoplasms and Endocrine	13.5	13.2	14.0
Gastrointestinal and Genitourinary	11.8	11.0	9.0
Respiratory System	9.0	9.6	8.8
Cardiovasculars	8.9	9.0	11.3
Vitamins and Nutrients	5.8	5.2	5.8
Dermatologicals	3.5	3.3	3.6
Biologicals	3.0	2.4	2.4
Diagnostic Agents	1.5	1.1	1.2
Other Pharmaceutical Preparations	4.5	8.5	4.0
TOTAL	100.0%	100.0%	100.0%

Source: PMA Annual Survey.

DISTRIBUTION OF SALES BY CUSTOMER TYPE

Table 1-4 shows the distribution, by class of customer, of human use, dosage form ethical pharmaceutical sales in the U.S. These sales are direct sales by the manufacturer. Retail pharmacies and hospitals, the usual sources of prescription drugs for patients, buy pharmaceuticals from wholesalers as well as directly from the manufacturer. However, manufacturers have shifted sales in recent years toward wholesalers and away from retailers.

TABLE 1-4

PERCENTAGE DISTRIBUTION OF U.S. ETHICAL PHARMACEUTICAL SALES
BY CLASS OF CUSTOMER
SELECTED YEARS 1972-1985

Class of Customer	1972	1974	1976	1978	1980	1982	1983	1985
Wholesalers	45.6%	45.2%	48.5%	51.4%	57.3%	59.6%	61.7%	67.3%
Retailers	29.4	28.1	26.4	22.8	20.8	18.0	17.2	16.0
Private Hospitals	14.6	15.6	14.8	16.0	12.7	13.7	12.6	8.8
State & Local Government Hospitals	4.7	4.8	4.5	4.2	4.1	3.8	3.5	2.5
Federal Hospitals	2.6	2.6	2.5	2.4	2.5	2.5	2.5	2.1
Other Federal Government	1.1	1.2	1.3	1.4	1.2	1.1	1.2	1.6
Practitioners	1.6	1.5	1.2	1.2	1.0	.8	.7	.7
Manufacturers, Repackagers, and Other Direct Sales	.4	1.0	.8	.6	.4	.5	.6	1.0
TOTAL	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%

Source: PMA Annual Survey (various years).

RETAIL SALES

Retail sales measure the value of drug products dispensed to the customer primarily through independent and chain retail pharmacies. The amount of money spent on prescription drugs is relatively small compared to the expenditures for other segments of health care. Sales of drugs and medical sundries in retail pharmacies accounted for only 6.7 percent of total national health expenditures in 1986. Retail pharmacy prescriptions alone accounted for about 3.9 percent of the national health dollar. Table 1-5 shows retail prescription drug sales of $18.9 billion in

1986, an increase of 182 percent over 1976. The value of retail sales includes the cost of a product to the pharmacy as well as the retail mark-up or charge for professional dispensing services.

TABLE 1-5

U.S. RETAIL PRESCRIPTION DRUG SALES
SELECTED YEARS
1974-1986

($ millions)

Year	Value of Sales
1986	$18,868.5
1985	17,257.5
1984	15,748.9
1983	13,941.6
1982	12,019.8
1981	10,321.7
1980	9,709.2
1978	7,932.2
1976	6,698.2
1974	5,664.1

Source: American Druggist, May 1979, May 1982, 1983, 1984, 1985, May 1986, and May 1987.

Retail sales figures are determined in part by the volume of prescriptions dispensed. Total prescriptions increased by 6.6 percent from 1976 to 1986 to 1.56 billion prescriptions (Table 1-6). However, the apparent small increase in retail prescriptions does not reflect the fact that the average prescription size is about 14 percent larger than it was in 1976. Table 1-6 demonstrates that the increases in total prescriptions in recent years are clearly the result of steady increases in refill prescriptions rather than new prescriptions, which show unstable growth in the past few years.[2]

[2] While significant changes have been made in the IMS, National Prescription Audit database, particularly in 1981 and 1983, it is unlikely that these changes had any effect on the trends shown in Table 1-6.

TABLE 1-6

U.S. PRESCRIPTION VOLUME
1976-1986

Year	New Rx's	Percent Change	Refills	Percent Change	Total Rx's	Percent Change
1976	740,848,000	- .1%	719,778,000	-3.8%	1,460,625,000	-2.0%
1977	726,675,000	-1.9	685,982,000	-4.7	1,412,657,000	-3.3
1978	743,552,000	2.3	653,336,000	-4.8	1,396,888,000	-1.1
1979	732,535,000	-1.5	633,323,000	-3.1	1,365,858,000	-2.2
1980	750,289,000	2.4	644,019,000	1.7	1,394,308,000	2.1
1981	737,797,000	-1.7	681,772,000	5.9	1,419,569,000	1.8
1982	768,189,000	4.1	729,994,000	7.1	1,498,183,000	5.5
1983	742,399,000	-3.4	765,735,000	4.9	1,508,134,000	.7
1984	750,118,000	1.0	781,630,000	2.1	1,531,748,000	1.6
1985	755,468,000	0.7	792,944,000	1.4	1,548,412,000	1.1
1986	784,483,000	3.8	773,028,000	-2.5	1,557,511,000	0.6

Source: IMS, National Prescription Audit, Various Years.

INTERNATIONAL OPERATIONS

The U.S. pharmaceutical industry is the largest of any nation. Although organized primarily to satisfy the large domestic market, American producers are exceptionally active in foreign trade and investment, and contribute substantially to the U.S. balance of payments.

The most comprehensive measure of the industry's contribution to the balance of payments emerges from data compiled by the International Trade Administration, U.S. Department of Commerce. These data include finished dosage form preparations, biologicals and medicinal chemicals which include drugs in bulk such as sulfonamide and acetylsalicylic acid, enzymes, certain inorganic medicinal chemicals and prepared culture media.

Since 1982, the balance of trade in pharmaceuticals has declined almost 39 percent, but remains positive at $764 million in 1986 (Table 1-7). The high value of the dollar in the early 1980s was a significant factor in the declining trade balance. The recent devaluation of the dollar is having an effect; the trade balance in pharmaceuticals declined only slightly in 1986.

According to United Nation's statistics for 1984 (Table 1-8), the United States is the world's largest exporter and importer of pharmaceutical products. U.S. pharmaceutical products are sold in nearly every country of the free world. Japan is by far the leading recipient of U.S. pharmaceutical exports, receiving over 20 percent of the total. Almost one-half of U.S. exports are sent to Europe, and over 20 percent go to developing countries (Table 1-9).

TABLE 1-7

FOREIGN TRADE OF THE UNITED STATES IN MEDICINALS AND PHARMACEUTICAL PREPARATIONS
1979-1986
($ Millions, f.a.s. values)

Year	Total Exports	Total Imports	Net Exports
1979	1634.1	874.6	759.5
1980	1966.1 (+20.3%)	930.7 (+ 6.4%)	1035.4 (+36.3%)
1981	2199.8 (+11.6%)	1048.7 (+13.0%)	1151.1 (+11.2%)
1982	2298.4 (+ 4.9%)	1051.3 (+ 4.0%)	1247.1 (+ 8.3%)
1983	2533.2 (8.8%)	1312.4 (+22.2%)	1220.8 (- 2.1%)
1984	2637.3 (4.1%)	1665.1 (+26.9%)	972.2 (-20.4%)
1985	2671.3 (1.3%)	1895.8 (13.9%)	775.5 (-20.2%)
1986	3086.5 (15.5%)	2322.2 (22.5%)	764.2 (- 1.5%)

(Percentages in the table above indicate changes from the preceding year.)

Source: International Trade Administration, U.S. Department of Commerce.

TABLE 1-8

WORLD TRADE IN MEDICINAL AND PHARMACEUTICAL PRODUCTS
1984
($ Thousands)

Countries	Exports	Imports	Balance of Trade
Leading Net Exporters			
United States	$2,759,028	$1,500,068	$1,258,960
Switzerland	1,508,181	431,081	1,077,100
Germany (F.R.)	2,160,007	1,224,511	935,496
United Kingdom	1,638,998	727,760	911,238
France	1,396,175	716,140	680,035
Denmark	397,818	213,269	184,549
Belgium	637,474	535,770	101,704
Netherlands	584,933	502,456	82,477
Yugoslavia	163,433	89,611	73,822
Sweden	373,887	307,332	66,555
Ireland	199,581	166,103	33,478
Singapore	121,990	104,345	17,645
Leading Net Importers			
Greece	$ 37,045	$122,655	$ -85,610
Portugal	38,328	124,826	-86,498
Korea Republic	32,443	119,126	-86,683
Indonesia	15,547	104,337	-88,790
Argentina	30,262	123,344	-93,082
Norway	41,606	134,245	-92,639
Mexico	58,187	156,447	-98,260
Thailand	10,413	114,102	-103,689
Austria	203,649	311,089	-107,440
Australia	93,230	219,292	-126,062
Egypt	10,460	151,913	-141,453
African Customs Union	13,992	182,276	-168,284
Canada	166,157	478,895	-312,738
Japan	355,476	1,258,490	-903,014

Source: 1984 International Trade Statistics Yearbook, U.N.

TABLE 1-9

FOREIGN TRADE OF THE UNITED STATES IN
MEDICINALS AND PHARMACEUTICAL PREPARATIONS BY WORLD AREAS
1980-1986
(Thousands of dollars, f.a.s. values)

Area	1980	1981	1982	1983	1984	1985	1986
Canada:							
Exports	$142,659	$150,031	$$66,099	$183,956	$185,230	$195,295	$205,330
Imports	22,043	22,410	26,701	28,120	26,934	29,742	32,953
Net U.S. Exports	$120,616	$127,621	$139,398	$155,836	$158,296	$165,553	$172,377
Latin American Republics:							
Exports	$271,560	$284,926	$271,512	$256,454	$280,425	$270,566	$327,334
Imports	29,834	34,268	32,491	27,955	27,248	32,471	40,805
Net U.S. Exports	$241,726	$250,658	$239,021	$228,499	$253,177	$238,095	$286,529
Other Western Hemisphere:							
Exports	$ 38,867	$ 29,009	$ 33,710	$ 35,014	$ 44,223	$ 41,686	$ 47,388
Imports	50,625	42,115	48,526	64,404	67,620	83,532	142,327
Net U.S. Exports	$(11,758)	$(13,106)	$(14,816)	$(29,390)	$(23,397)	$(41,846)	$(94,939)
United Kingdom							
Exports	$108,320	$108,238	$117,445	$172,584	$167,537	$157,659	$191,905
Imports	117,205	145,666	157,768	269,293	366,640	366,196	436,211
Net U.S. Exports	$ (8,885)	$(444,428)	$(40,323)	$(66,709)	$(199,103)	$(208,537)	$(244,306)
E.E.C. Countries (inc. U.K.):							
Exports	$717,202	$773,452	$790,826	$923,755	$929,074	$966,466	$1,158,768
Imports	528,333	602,107	587,430	765,382	1,050,760	1,053,001	1,177,309
Net U.S. Exports	$ 18,869	$171,345	$203,396	$158,373	$(121,686)	$(86,535)	$(18,541)
OECD Countries of Europe:							
Exports	$897,982	$952,122	$976,019	$1,155,205	$1,075,675	$1,202,085	$1,487,962
Imports	643,497	722,821	717,382	910,041	1,241,166	1,359,862	1,541,424
Net U.S. Exports	$254,485	$229,301	$258,637	$ 245,164	$ (165,491)	$ (157,777)	$ (53,462)
Japan:							
Exports	$334,316	$442,960	$504,106	$537,023	$563,339	$581,081	$637,009
Imports	127,347	159,465	148,505	188,133	189,728	201,318	321,220
Net U.S. Exports	$206,969	$283,495	$355,601	$348,890	$373,611	$379,763	$315,789

TABLE 1-9
(Continued)

FOREIGN TRADE OF THE UNITED STATES IN
MEDICINALS AND PHARMACEUTICAL PREPARATIONS BY WORLD AREAS
1980-1984

(Thousands of dollars, f.a.s. values)

Area	1980	1981	1982	1983	1984	1985	1986
Other Asia:*							
Exports	$183,224	$228,173	$246,235	$247,356	$271,566	$254,431	$246,546
Imports	20,968	25,717	28,566	33,838	49,446	105,138	155,405
Net U.S. Exports	$162,256	$202,456	$217,669	$213,518	$222,120	$149,293	$ 91,141
Australia & Oceania:							
Exports	$ 39,733	$ 50,264	$ 48,210	$ 58,985	$ 65,436	$ 66,448	$ 65,745
Imports	2,171	3,796	8,042	11,801	12,262	17,583	13,400
Net U.S. Exports	$ 37,562	$ 46,468	$ 40,168	$ 47,184	$ 53,174	$ 48,865	$ 52,345
Africa:							
Exports	$ 35,175	$ 42,115	$ 39,261	$ 45,570	$ 52,396	$ 42,686	$ 52,397
Imports	,636	1,011	1,211	1,357	1,917	3,175	3,199
Net U.S. Exports	$ 34,539	$ 41,104	$ 38,050	$ 44,213	$ 50,479	$ 39,511	$ 49,198
Principal Developing Arèas:**							
Exports	$528,826	$584,223	$590,718	$584,394	$648,610	$620,229	$682,933
Imports	102,063	103,111	110,794	127,554	146,231	275,044	401,790
Net U.S. Exports	$426,763	$481,112	$479,924	$456,840	$502,379	$345,185	$281,143
World Total:***							
Exports	$1,966,064	$2,199,811	$2,298,399	$2,533,200	$2,637,329	$2,671,332	$3,086,547
Imports	930,669	1,048,729	1,051,257	1,312,394	1,665,085	1,895,831	2,322,288
Net U.S. Exports	$1,035,395	$1,151,082	$1,247,142	$1,220,806	$ 972,244	$ 775,501	$ 764,259

*Excludes Japan and Communist Asia.
**Based on combined figures for Latin America, other Western Hemisphere, Asia other than Japan and Communist areas, and Africa.
***Totals include Communist areas not shown separately above.

Source: International Trade Administration, U.S. Department of Commerce.

In large part, U.S. exports of pharmaceutical products consist of ingredients and intermediate products sent abroad to be processed and packaged. This practice reflects practical considerations such as convenience in satisfying a market, the need to label medicines in a foreign language and the desire to meet the preferences of local doctors and patients for certain dosage forms. The passage of the Omnibus Health Act in 1986 opened new exporting opportunities for pharmaceutical firms. Under the new law, firms can now export drugs that have not been approved by the U.S. Food and Drug Administration to a select list of countries that have approved the drugs. These drugs must be under clinical study here in the U.S. to be eligible for exporting.

In other cases, manufacturing abroad is encouraged by tariff or non-tariff barriers to imports, national laws, or other policies of a foreign country that make it difficult or impossible to market a product unless it is largely produced within its boundaries. In most instances, production in foreign countries has been a means of achieving sales that otherwise would not have been possible. Through foreign subsidiaries and affiliates, many U.S. companies increase their shipments of bulk materials and ingredients as well as supplies and equipment. This helps to sustain or expand U.S. domestic employment.

The production and sales of major companies through their networks of affiliates in other countries have contributed significantly to the industry's international importance. U.S. sales abroad, directly and through foreign branches and subsidiaries, exceeded $10 billion in 1985. These operations abroad have made important contributions to the economies of the countries in which the subsidiary operations are located. Foreign subsidiaries of U.S. firms establish local facilities that provide training and employment for local workers, add to tax revenues, contribute to the balance of payments of the host country, support local corollary industries, and reinvest earnings in the host country. In turn, various Swiss, West German, French and British firms have long owned and operated plants in the U.S.

Many PMA companies have subsidiaries or jointly-owned affiliates in other countries, and many other member companies engage in international operations through licensing and exporting. Sales achieved through manufacturing abroad greatly exceed direct exports from the U.S. (Table 1-10). Combined sales abroad in 1985 were more than double the total ten years earlier.

Although most pharmaceutical sales abroad by U.S. companies are made to other advanced countries, U.S. companies also have significant pharmaceutical activities in developing countries. Many U.S. firms enjoy long-established relationships with Latin America and several countries in Asia and Africa. In fact, the U.S. pharmaceutical industry has invested heavily in

TABLE 1-10

FOREIGN SALES OF ETHICAL PHARMACEUTICALS BY U.S.-OWNED PMA MEMBER FIRMS 1965-1985

($ Millions)

Year	Total Foreign Sales	Sales Abroad	Exports
1965	$ 1,097.7	$ 917.7	$ 180.0
1966	1,275.6	1,074.6	201.0
1967	1,498.0	1,281.5	216.5
1968	1,650.7	1,424.8	225.9
1969	1,856.8	1,559.5	297.3
1970	2,151.8	1,807.7	344.1
1971	2,387.9	2,005.5	382.4
1972	2,806.3	2,428.4	377.9
1973	3,278.0	2,712.4	565.6
1974	3,940.2	3,206.2	734.0
1975	4,796.3	4,042.6	753.7
1976	5,293.7	4,398.9	894.8
1977	5,810.5	4,862.9	947.6
1978	7,091.0	6,026.3	1,064.7
1979	8,564.8	7,410.0	1,154.8
1980	10,515.4	9,296.1	1,219.3
1981	10,658.4	9,264.5	1,393.9
1982	10,667.4	9,221.1	1,446.3
1983	10,411.2	9,075.5	1,335.7
1984	10,450.9	9,110.1	1,340.8
1985	10,872.3	9,315.4	1,556.9

"Exports" includes shipments to subsidiaries abroad as well as exports to nonaffiliated firms. These data are based on ethical pharmaceutical sales provided by member companies and are not directly comparable with Commerce Department or United Nations trade data.

"Sales Abroad" refers to sales in a foreign area by subsidiaries or other corporate operations, adjusted to eliminate double counting of intrafirm transactions. Also excluded are sales outside the U.S. by foreign-owned firms which have subsidiaries in the U.S.

Source: PMA Annual Survey, various years.

developing countries, employing thousands of local workers and helping build technological expertise.

Earning rates vary in foreign countries because many foreign governments impose price controls, and because of different risks and competitive factors. In addition to direct earnings from sales, patent royalties, fees received for management and engineering services, and other remittances from abroad help the industry improve the U.S. balance of payments.

CONCENTRATION

The Bureau of the Census compiles statistics on concentration ratios for over 400 American industries in the quinquennial Census of Manufacturers. These statistics include the share of total sales held by the four largest, eight largest and 20 largest firms in each industry.

Some industries, such as automobile or primary aluminum, are highly concentrated in that only a few companies account for a major share of industry sales. Other industries, such as concrete or commercial printing, have very low rates of concentration. The four-firm concentration ratio for the pharmaceutical industry ranks in the bottom 40 percent among the total of approximately 450 U.S. industries examined by the Bureau of Census (Table 1-11).

Using marketing research data, it is also possible to look at concentration ratios in terms of market share of new and refill prescription dollars. Table 1-12 includes data for 1978 through 1986. These data indicate that concentration in the industry has been relatively stable, declining only slightly in recent years.

TABLE 1-11

CONCENTRATION RATIOS FOR FIRMS MANUFACTURING PHARMACEUTICAL PREPARATIONS (SIC 2834)
Selected Years, 1958-1982

		Percent of value of shipments accounted for by:		
Year	Number of Establishments	4 Largest Companies	8 Largest Companies	20 Largest Companies
1958	1,114	25%	43%	71%
1963	1,011	22	37	71
1967	875	24	40	70
1972	756	25	43	73
1977	756	25	41	70
1982	683	26	41	67

Source: 1982 Census of Manufacturers, Pub.MC77-Sr-9, Subject Series, Bureau of Census, U.S. Department of Commerce, 1986.

TABLE 1-12

COMPETITION FOR NEW U.S. PRESCRIPTIONS
MEASURED IN TOTAL PRESCRIPTION DOLLARS

1978-1986

Company Group	Percentage of New and Refill Prescription Dollars [a,b,c,d]								
	1978	1979	1980	1981	1982	1983	1984	1985	1986
Leading Company	8.8%	10.1%	9.8%	9.2%	8.4%	8.3%	8.4%	7.5%	6.8%
4 Largest	31.4	32.3	31.6	30.5	29.5	29.6	29.2	27.1	25.0
8 Largest	49.4	50.2	50.1	49.8	48.9	48.4	47.7	44.7	43.3
20 Largest	81.5	81.9	81.8	81.9	79.4	78.4	77.0	74.1	72.6
50 Largest	98.2	98.8	98.8	98.7	96.7	96.1	96.2	94.3	95.7
All Companies	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%

a "Unspecified" prescriptions not included in calculations for the years 1978-1981. The Unspecifieds accounted for 6.4 percent to 6.8 percent of total Rx dollars between 1978 and 1981.

b Pharmacy cost level.

c Data for 1982-1986 are for prescriptions as they were dispensed, not prescribed as was the case for earlier years.

d Sales of subsidiaries were combined with parent corporation sales in making calculations.

Source: National Prescription Audit, IMS America, Ltd.

One additional measure of industry concentration--the Herfindahl-Hirschman Index (HHI)--has been used to examine the effects of proposed mergers. This measure has been advocated as the appropriate market power measure for antitrust purposes.[3]

Table 1-13 shows the HHI values[4] computed for 1978 through 1986, using the same data upon which the concentration ratios of Table 1-12 were based. In examining the impact of merger activity, the critical value of the HHI that would trigger concern about a particular merger is not well-established. However, a value of 1000 is generally viewed as being unlikely to be challenged. As Table 1-13 shows, the pharmaceutical industry HHI is less than half of this usually accepted value and in fact has declined by 23 percent since 1980.

TABLE 1-13

PHARMACEUTICAL INDUSTRY CONCENTRATION
HERFINDAHL-HIRSCHMAN INDEX VALUES
1978-1986

Year	Index Value
1978	440
1979	453
1980	446
1981	439
1982	414
1983	411
1984	394
1985	368
1986	342

Source: PMA calculations based on data from National Prescription Audit data, IMS, America.

EARNINGS

In a very real sense, earnings represent the end of the research-marketing-physician-pharmacist-consumer chain. Earnings also provide the capital necessary to finance a new cycle of research and so can be considered a beginning as well.

[3] Department of Justice Antitrust Division-Merger Guidelines, Federal Register, (June 1982), 28494-28502.

[4] The HHI is computed by squaring the market share for each firm, expressed in percent, and summing the result. This sum is then multiplied by 10,000 to express the HHI value in whole numbers.

By most measures, the pharmaceutical industry is profitable, with earnings traditionally above the average for all manufacturing industries. However, the concept of profitability is not sufficiently well-defined to rely on a single measure of profitability. No single measure conveys appropriate information to all economic agents interested in the performance of the industry. The results obtained using accounting data may differ from those obtained using capital market data.

Some commonly used accounting measures of profitability are: return on sales, return on stockholders' equity, return on capital employed, and return on assets. Return to investors[5] is an example of a capital market measure. To illustrate how relative profitability is sensitive to the measure of profitability chosen, consider the Fortune 500 Corporations for 1980-1986[6] and the following three measures of profitability.

(i) Return on Sales
(ii) Return on Stockholders' Equity
(iii) Return to Investors

Each firm in the Fortune 500 is classified into one of 27 industries including pharmaceuticals. The medians for the pharmaceutical industry and "all industries" for each of the three measures of profitability used in Fortune are given in Table 1-14.

The relative profitability of the pharmaceutical industry depends on the measure of profitability used. As Table 1-15 illustrates, the pharmaceutical industry appears to be relatively profitable if return on sales and return on stockholders' equity are used as measures of profitability, but the industry is ranked closer to the middle of the set of 27 industries when return to investors is used as a measure of profitability.

The question of which measures of profitability are most appropriate for evaluating an industry remains a matter of personal judgment rather than logical derivation. However, policy discussions will often focus on measures that use readily available accounting data on sales, net income (earnings), and stockholders' equity. Earnings as a percent of sales both before and after taxes, are displayed in Table 1-16. Earnings as a percent of stockholders' equity are shown in Table 1-17.

Based on these measures of profitability, the pharmaceutical industry is among the most profitable industries. However, the industry also leads in terms of the percentage of its sales reinvested in R&D which involves considerable risks. The industry invested an estimated 15.0 percent of its sales in research and development in 1986.

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[5] Return to investors includes both stock price appreciation and dividend yield.

[6] There are 20-25 pharmaceutical firms included in each edition of Fortune 500.

TABLE 1-14

MEDIAN RETURN (%)
PHARMACEUTICAL/ALL INDUSTRIES

Year	Sales	Equity	Investors
1980	9.1/4.8	17.9/14.4	Not Available
1981	9.1/4.6	18.0/13.8	3.07/-.35
1982	9.9/3.6	16.9/10.9	32.82/21.22
1983	10.4/3.8	17.5/10.7	7.18/30.21
1984	10.0/4.5	18.1/13.6	7.78/.75
1985	10.4/3.9	15.6/11.6	11.47/24.13
1986	13.1/4.1	23.6/11.6	27.90/15.50

Source: Fortune, various issues.

TABLE 1-15

RANK OF THE PHARMACEUTICAL INDUSTRY
(PROFITABILITY)
AMONG 27 INDUSTRIES

Year	Sales	Equity	Investors
1980	2	4	Not Available
1981	2	3	12
1982	1	1	11
1983	1	2	21
1984	1	3	6
1985	1	6	20
1986	1	1	6

Source: Fortune, various issues.

The risks involved in the research process are highlighted by the uncertainty about whether large investments in R&D will yield commercially successful products. Risk factors are not adequately taken into account in profitability comparisons based on traditional earnings measures. The U.S. Department of Commerce

TABLE 1-16

COMPARATIVE EARNINGS STATISTICS
EARNINGS AS A PERCENT OF SALES
1970-1986[a]

Year	Before Taxes		After Taxes	
	Pharmaceutical Industry	All Manufacturing	Pharmaceutical Industry	All Manufacturing
1970	17.2%	6.8%	9.4%	4.0%
1971	17.0	7.1	9.5	4.2
1972	18.1	7.5	10.3	4.3
1973	17.8	8.0	10.2	4.7
1974	19.3	8.7	12.2	5.5
1975[b]	19.3	7.5	12.3	4.6
1976	19.0	8.7	12.2	5.4
1977[b]	19.2	8.7	12.1	5.3
1978	19.1	8.9	12.5	5.4
1979[b]	18.6	8.9	12.9	5.7
1980[b]	18.6	7.7	13.2	4.8
1981[b]	15.6	7.4	10.9	4.8
1982[b]	17.9	5.3	13.1	3.5
1983	19.3	6.3	13.4	4.0
1984	19.1	7.1	13.3	4.6
1985	14.6	5.9	9.8	3.8
1986	20.7	5.8	14.5	3.7

[a] Ratios were calculated using fourth quarter reports.
[b] First quarter reports for the succeeding year were used to calculate these ratios.

Source: Quarterly Financial Report (for manufacturing, mining, and trade corporations), 1970--First Quarter 1982, U.S. Federal Trade Commission; Second Quarter, 1982-1986, U.S. Department of Commerce.

has noted that "in this respect, some economists have shown that profitability analysis in the pharmaceutical industry is misleading for several reasons. First, the accounting profits or rates of return of an individual project may be significantly higher during the early years of new drug sales. Second, there is a long time lag, five to ten and sometimes many more years, between the investment and the return on the investment.'"

TABLE 1-17

COMPARATIVE EARNINGS STATISTICS
EARNINGS AS A PERCENT OF STOCKHOLDERS' EQUITY
1970-1986[a]

	Before Taxes		After Taxes	
Year	Pharmaceutical Industry	All Manufacturing	Pharmaceutical Industry	All Manufacturing
1970	32.4%	15.7%	17.6%	9.3%
1971	31.2	16.5	17.9	9.7
1972	32.8	18.4	18.6	10.6
1973	33.1	21.8	19.0	12.8
1974	29.7	23.3	18.8	14.9
1975[b]	27.8	18.9	17.8	11.6
1976	28.2	22.7	18.1	14.0
1977[b]	28.9	23.2	18.2	14.2
1978	28.6	24.5	18.8	15.0
1979[b]	27.9	25.7	19.3	16.5
1980[b]	27.9	22.0	19.9	14.0
1981[b]	24.2	21.4	16.9	13.7
1982[b]	27.0	14.1	19.7	9.3
1983	29.2	16.4	20.3	10.6
1984	28.9	19.1	20.2	12.4
1985	22.5	15.8	15.2	10.1
1986	32.6	14.9	22.9	9.6

[a] Ratios were calculated using fourth quarter reports.
[b] First quarter reports for the succeeding year were used to calculate these ratios.

Source: Quarterly Financial Report (for manufacturing, mining, and trade corporations), 1970--First Quarter 1982, U.S. Federal Trade Commission; Second Quarter, 1982-1986, U.S. Department of Commerce.

' A Competitive Assessment of the U.S. Pharmaceutical Industry, International Trade Administration, U.S. Department of Commerce, December, 1984.

EMPLOYMENT AND EARNINGS

In 1983, the U.S. pharmaceutical industry employed 306,600 persons worldwide. Employment abroad by U.S. firms represented 48.3 percent of the worldwide figure in 1983, but declined to 47.4 percent in 1985 (Table 1-18). Table 1-19 shows the distribution of pharmaceutical employees in the U.S.

TABLE 1-18

U.S. ETHICAL PHARMACEUTICAL INDUSTRY EMPLOYMENT

1983 AND 1985

	Number of Workers	
	1983	1985
United States	158,800	164,400
Foreign	148,000	148,300
TOTAL	306,600	312,700

Source: PMA Annual Survey, 1983-1985.

TABLE 1-19

ETHICAL PHARMACEUTICAL EMPLOYMENT IN THE U.S.

1983 and 1985

	1983	1985
Production Workers	62,500	58,600
Marketing	40,400	44,600
Medical Research & Development	31,800	35,800
Administrative	17,300	18,100
Distribution & Other	6,600	7,300
TOTAL U.S. Employment	158,600	164,400

Source: PMA Annual Survey, 1983-1985.

PRODUCTIVITY

Employees in the pharmaceutical industry have increased productivity faster than employees engaged in other lines of business. From 1975 to 1985, pharmaceutical productivity increased 25 percent. For all non-farm businesses, the increase was 9.3 percent.

TABLE 1-20

INDEXES OF PRODUCTIVITY
U.S. PHARMACEUTICAL INDUSTRY AND U.S. PRIVATE NON-FARM BUSINESS
1971-1986

(1977 = 100)

	Index of Output (Production) Per Employee Hour	
Year	Pharmaceutical Industry	Non-Farm Business
1971	81.0	92.4
1972	86.8	94.8
1973	84.8	96.3
1974	90.3	94.2
1975	92.5	96.2
1976	98.4	98.3
1977	100.0	100.0
1978	98.5	100.8
1979	105.3	99.2
1980	106.0	98.9
1981	104.2	99.8
1982	107.0	99.6
1983	114.4	103.2
1984	112.6	104.8
1985	115.6	105.1
1986	Not available	105.7

Source: Office of Publications, U.S. Bureau of Labor Statistics, U.S. Department of Labor, (various statistical series).

CHAPTER II

THE INDUSTRY'S COMMITMENT TO RESEARCH AND DEVELOPMENT

RESEARCH AND DEVELOPMENT EXPENDITURES

The pharmaceutical industry has invested over $36 billion in pharmaceutical research and development (R&D) since the early 1940s. This research commitment led to the discovery of more than 1,100 new chemical entities that have helped prevent disease, cure illness, prolong life and reduce the cost of being sick. Total worldwide R&D spending by PMA member companies was $3.6 billion in 1984 and $4.1 billion in 1985. Spending for 1986 is estimated at $4.6 billion and will exceed $5.0 billion in 1987. These figures include spending for both human-use and veterinary products.

Research by U.S. firms abroad accounted for $699 million in 1985--17.1 percent of the total amount. For 1986, U.S. R&D abroad was estimated at $825 million or 17.8 percent of total R&D spending (Figure 2-1). In 1970, research abroad represented only eight percent of total R&D spending by U.S. firms.

Companies finance almost all of their R&D, although they also conduct a very limited amount of research under contract with the federal government. Over the last 17 years, these government funded projects involved annual expenditures ranging as high as $14 million. In 1985, federally-financed R&D amounted to $8.0 million, or less than one percent of the industry total. The estimated total for federal funds in 1986 was $8.2 million.

R&D-TO-SALES RATIO

A key measure of the industry's continued commitment to research is the ratio of annual R&D expenditures to dollar volume of pharmaceutical sales. Expressed as a percentage, the ratio has been above ten percent each year since 1965 and since 1980 has increased by 28 percent from 11.7 percent to 15.0 percent (Table 2-1).

ALLOCATION OF RESEARCH FUNDS

Allocation to Product Innovation. In 1985, almost 84 percent of U.S. R&D expenditures were devoted to the quest for new scientific knowledge and the development of new therapies. Improvement of existing products represented the remaining 16 percent.

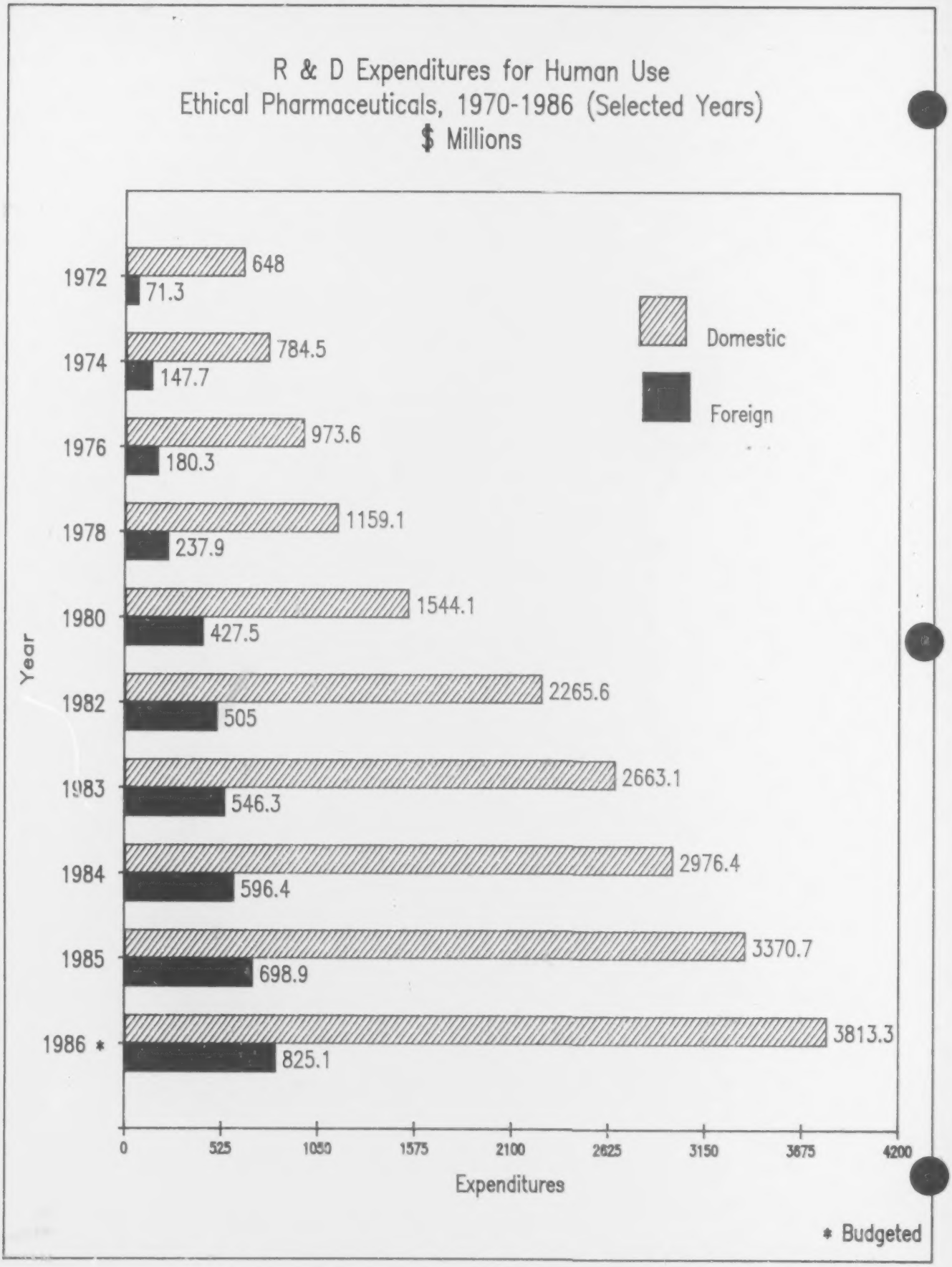

R & D Expenditures for Human Use
Ethical Pharmaceuticals, 1970-1986 (Selected Years)
$ Millions
Year
1972
1974
1976
1978
1980
1982
1983
1984
1985
1986 *
648
71.3
784.5
147.7
973.6
180.3
1159.1
237.9
1544.1
427.5
2265.6
505
2663.1
546.3
2976.4
596.4
3370.7
698.9
3813.3
825.1
Domestic
Foreign
0
525
1050
1575
2100
2625
3150
3675
4200
Expenditures
* Budgeted

Table 2-1
U.S. PHARMACEUTICAL R&D EXPENDITURES
AS A PERCENTAGE OF U.S. PHARMACEUTICAL SALES*
1965-1986

YEAR	PERCENT	YEAR	PERCENT
1965	10.2%	1976	11.3%
1966	10.8	1977	11.3
1967	11.3	1978	11.1
1968	10.9	1979	11.4
1969	11.1	1980	11.7
1970	11.6	1981	13.1
1971	12.1	1982	13.8
1972	11.8	1983	14.4
1973	11.4	1984	14.4
1974	11.3	1985	14.8
1975	11.6	1986	15.0

* Includes U.S. sales plus exports.

Source: PMA Annual Survey Report.

ALLOCATION BY PRODUCT CLASS

Survey data for 1985 show that the pharmaceutical industry targets its research and development on major health problems. For example, about 72 percent of U.S. R&D expenditures were directed to finding new drugs to treat cardiovascular diseases, infections, neoplasms and central nervous system problems. Expenditures were highest for drugs acting on the cardiovascular system and anti-infectives.

Table 2-2 shows the allocation of funding among all product classes, with each class representing drugs useful against a common set of health problems, symptoms, or diseases.

FOREIGN RESEARCH AND DEVELOPMENT

Since 1967, the share of U.S. company-funded R&D work carried out overseas by U.S. firms more than doubled. One reason for this is that costs are lower in some other countries. Another factor is the lengthy approval process for new drugs in the U.S. All major countries have strict rules for approving new pharmaceutical products, but few--if any--countries take as long as the U.S.

Table 2-3 shows the recent trend in foreign research expenditures by domestic firms. Figure 2-2 shows graphically the historical shift of research activity from the U.S. to foreign countries.

TABLE 2-2
U.S. PHARMACEUTICAL R&D EXPENDITURES BY PRODUCT CLASS
1983 - 1985

Ranking 1983	Ranking 1985	Product Class	Percentage Share of R&D Dollar 1983	Percentage Share of R&D Dollar 1985
1	1	Cardiovasculars	22.7%	25.8%
3	2	Neoplasms, Endocrine System & Metabolic Diseases	16.3	18.1
2	3	Anti-infectives	16.8	14.9
4	4	Central Nervous System & Sense Organs	12.8	12.9
5	5	Gastrointestinal & Genitourinary System	6.0	5.8
6	6	Respiratory	5.1	5.7
8	7	Biologicals	2.1	2.6
7	8	Dermatologicals	2.2	1.7
9	9	Vitamins	1.3	1.1
10	10	Diagnostic (in vivo)	.8	.7
		Other Human Use Drugs	9.2	6.6
		Veterinary Preparations	4.2	3.7
		Veterinary Biologicals	.5	.4
			100.0%	100.0%

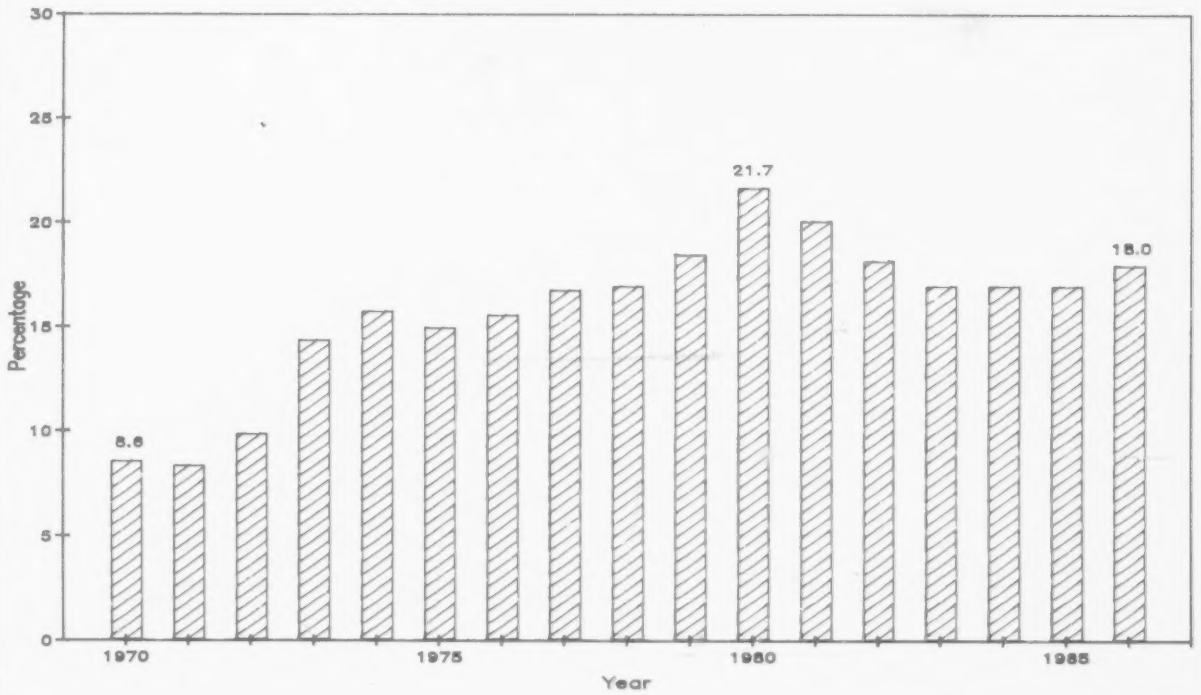
Source: PMA Annual Survey Report.

TABLE 2-3
R&D EXPENDITURES OF U.S. COMPANIES IN FOREIGN COUNTRIES
1983-1986
($ Millions)

	1983	1984	1985	1986*
Spent within firms:				
Human Use	$439.4	$480.7	$564.7	$647.8
Veterinary Use	18.5	14.3	15.4	18.6
Spent outside firms:				
Human Use	86.0	95.4	112.4	150.2
Veterinary Use	2.4	6.0	6.4	8.5
Total Expenditures:				
Human Use	525.4	576.1	677.1	798.0
Veterinary Use	20.9	20.3	21.8	27.1
Grand Total:				
Human and Veterinary	$546.3	$596.4	$698.9	$825.1

* Budgeted.
Source: PMA Annual Survey Report.

Figure 2-2
Percentage of U.S. Company-Funded
Research and Development Conducted Abroad
1970-1986 *



NEW DISCOVERY

Introduction of New Products in the United States. Since 1940, 1,178 new single-chemical entities (NCE's) have been introduced into the U.S. market. The annual number of introductions since 1962 has been only about one-third to one-half of the levels achieved during the 1950s (Table 2-4).

Changes in the regulatory process since the late 1950s have increased the time needed to test new drugs. From seven to ten years elapse between the discovery of a new drug and FDA approval for marketing. This compares with an average of approximately two years prior to the 1962 Amendments to the Food, Drug, and Cosmetic Act.

As the development time for new drugs has increased, so has the cost of R&D per new drug introduced. A large part of industry R&D expenditures, including basic research and the cost of development for projects that must be abandoned for reasons of lack of effectiveness or excessive risks, cannot be allocated to specific products. For this reason, it is difficult to estimate the full R&D costs for a specific product.

TABLE 2-4

NEW SINGLE ENTITY DRUG INTRODUCTIONS TO U.S. MARKETS
1940-1986

Year	Number of Entities	Year	Number of Entities
1940	14	1963	16
1941	17	1964	17
1942	13	1965	25
1943	10	1966	13
1944	13	1967	25
1945	13	1968	12
1946	19	1969	9
1947	26	1970	16
1948	29	1971	14
1949	38	1972	10
1950	32	1973	17
1951	38	1974	18
1952	40	1975	15
1953	53	1976	14
1954	42	1977	16
1955	36	1978	23
1956	48	1979	15
1957	52	1980	13
1958	47	1981	19
1959	65	1982	26
1960	50	1983	22
1961	45	1984	15
1962	24	1985	20
		1986	24
		TOTAL:	1178

Source: PMA Analysis of Paul De Haen data.

Table 2-5 summarizes the results of six studies that examined the costs of discovering and developing new products in the pre-1962 and post-1962 periods, excluding the costs of capital. These studies document the substantial increase in the cost of bringing new drugs to market. The studies show that post-1962 costs averaged about seven times pre-1962 costs.

TABLE 2-5

RESEARCH AND DEVELOPMENT COSTS* PER NCE DRUG
PRE-1962 VS. POST-1962**

(1980 Dollars)

	Pre-1962 ($ Million)	Post-1962 ($ Million)
Schwartzman	$3.7	$48.6
Sarett	3.4	25.9
Mansfield/Schnee	3.1	-
Clymer	-	56.5
Hansen	-	47.6
Baily	16.0	-

* Excluding the cost of capital.
** Studies examined drugs approved from 1963 through 1975.

Source: Hutt, Peter Barton, The Importance of Patent Term Restoration to Pharmaceutical Innovation, Health Affairs, Spring, 1982.

The study by Hansen is of particular interest. He used an accounting approach and studied R&D expenditures for a sample of new drugs from 1963 through 1975. Because R&D expenditures for a new drug are made over a period of years, these expenditures were capitalized in the study. Hansen found an average cost of $54 million (1976 dollars), including the cost of capital.

Hansen also considered the costs for the major phases of the R&D process--preregulatory and regulatory. The regulatory phase begins with the Investigational New Drug (IND) Exemption required to begin tests in human beings. Hansen estimated that pre-IND expenditures are about equal to those incurred during the post-IND phase.

A new study by Steven Wiggins at Texas A&M University, based on new chemical entities approved between 1970 and 1985, estimates that the total cost for an approved new drug is $125 million in 1986 dollars.[1] Like the Hansen study, this new analysis accounts for the opportunity costs of investing funds several years before a drug can be marketed. The increasing cost of developing a new drug is in part attributable to the increasing research focus on chronic conditions. Drugs intended to treat these conditions require more extensive testing.

[1] Wiggins, Steven N., The Cost of Developing a New Drug, PMA, 1987.

NEW DRUG INTRODUCTIONS: U.S. VS. FOREIGN

Table 2-6 lists for each year the number of introductions by country where the headquarters of the company or institution developing the new drugs were located. A total of 1,713 drugs were introduced from 1961 through 1986. U.S. companies were responsible for 411 or 24.0 percent of the total. Table 2-6 also shows a declining trend worldwide in the number of new drugs introduced each year until 1985 when introductions rose to 53 from 37 the previous year.

Drug introductions by country where each new drug was first marketed are shown in Table 2-7. The results show that only 7.6 percent of the 1,713 new drugs were marketed first in the U.S., 19.0 percent were first introduced in France, 14.4 percent in West Germany, and 13.1 percent in Japan. In 1986, nearly half the new drugs introduced were marketed first in Japan.

A similar study[2] conducted by the U.S. Food and Drug Administration examined annual introductions of original molecules in five countries--France, Germany, Italy, the United Kingdom, and the U.S. The study concluded that about 32 percent of all new drugs introduced in the five countries eventually are marketed in the U.S. About 46 percent of the drugs are introduced in the U.K., while France, Italy and Germany each get 60 to 70 percent of the total number of drugs introduced in the five countries.

The FDA study also looked at the "drug lag" in the five countries--i.e., the length of time that elapses between first introduction of a drug and its introduction in another country. For drugs first introduced between 1960 and 1962, approximately 1.7 years elapsed on average before introduction in the U.S. market. The lag time in the U.S. increased to four years for drugs introduced in the late 1960s, but declined in the early 1970s to about 2.2 years--a figure consistent with the experience for France, Germany and the U.K.

NEW DRUGS, 1940-1986

The long-standing leadership of the U.S. in drug innovation is reflected by the fact that about 62 percent of the new chemical entities introduced in the country since 1940 were U.S. discoveries (Table 2-8). In the U.S. over 90 percent of the new drugs were discovered by private industry.

Table 2-9 shows the distribution of introductions by therapeutic class. Since 1940, the therapeutic class that had the largest number of new chemical entities introduced was anti-infectives, with a total of 222 products.

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[2] A Historical Look at Drug Introductions on a Five-Country Market, OPE Study 60, Food and Drug Administration, March, 1982.

TABLE 2-6
NEW DRUG INTRODUCTIONS BY YEAR AND COUNTRY OF ORIGIN
1961-1986

Year of Introduction	U.S.	France	West Germany	Japan	Italy	Switzerland	Eastern Block	Great Britain	Other countries(a)	Annual New Introductions
1961	31(1)	12	11	7	4	12(1)	3	6	9(1)	93
1962	20	21	15	4	7	8	-	4	14	93
1963	22(1)	21	17(1)	12	2	7	2	9	8	99
1964	15	8	14	8	4	6	5	4	6	70
1965	13	14	10	13	6	7	2	4	4	73
1966	22	19	7	8	3	3	8	4	10	84
1967	20(1)	19	8	7	5	8	9	5(1)	7	87
1968	20(2)	17(1)	12(1)	7	7(1)	5(1)	5	4	10	84
1969	18(1)	23	11	5	9	3	9	3(1)	5	85
1970	21(1)	18	7(1)	7	1	6	4	2	6	71
1971	25	16	5	11	7	6	9	2	10	91
1972	14	13	4	9	9	3	8	3	4	67
1973	10	18	14(1)	1	8	9(1)	9	3	6	77
1974	17(1)	13	9(1)	14	4	5	4	4	8	77
1975	15	7	12	8	5	8(1)	11	4	4(1)	73
1976	17(1)	8	9(1)	2	7	2	5	3	8	60
1977	14	6	13	7	11	3	1	6	6	67
1978	12	10	7(1)	7	4	4(1)	2	4	5	54
1979	14	6	7	7	7	-	1	-	3	45
1980	13(1)	2	9(1)	11(1)	9	4(2)	-	-	3(1)	48
1981	(data not available for 1981)									
1982	8	5	1	10	3	4	1	-	7	39
1983	10	3	9	8	1	4	-	2	2	39
1984	7	5	1	11	5	4	-	2	2	37
1985	18	4	4	14	6	1	-	3	3	53
1986	15(3)	3	7	17(2)	2	-	-	3	3(1)	47
Total	411 (13)	291 (1)	223 (8)	215 (3)	136 (1)	122 (7)	98	84 (3)	153 (4)	1,713

[a] Argentina, Australia, India, Canada, Portugal, Scandinavia, Benelux, Spain, Austria, and Finland.

Note: Figures in parentheses signify substances developed simultaneously in two countries. The figure in parentheses is always included in the preceding number of substances.

Source: E. Reis-Arndt, Medical Marketing & Media (August 1983): 12 (1961-1980 figures); and "World Drug Introductions," Scrip, various issues (1982-1986 figures). No 1981 figures were available.

TABLE 2-7

NUMBER OF NEW DRUGS, BY YEAR AND COUNTRY OF FIRST MARKETING
1961-1986

Year of Introduction	France	West Germany	Japan	Great Britain	Italy	U.S.	Eastern Block	Switzerland	Other Countries(a)	Annual First Introductions
1961	10	12	6	9	4	27	3	8	14	93
1962	24	18	4	6	11	12	–	5	13	93
1963	20	24	12	17	2	7	2	6	9	99
1964	16	14	5	7	1	7	5	4	11	70
1965	16	14	13	4	6	4	2	4	10	73
1966	24	12	8	8	3	6	8	1	14	84
1967	19	12	11	10	7	5	9	5	9	87
1968	19	15	7	11	4	2	5	4	17	84
1969	25	13	7	7	8	3	8	2	13	85
1970	21	6	8	4	5	6	4	4	13	71
1971	15	5	11	8	7	6	9	6	24	91
1972	14	4	9	7	9	4	8	2	10	67
1973	21	6	2	6	6	6	9	4	17	77
1974	14	5	15	11	5	4	3	4	16	77
1975	10	7	8	5	8	3	10	8	14	73
1976	9	5	2	6	6	2	5	2	23	60
1977	4	18	7	7	13	3	1	3	9	67
1978	15	7	7	6	4	3	2	3	7	54
1979	9	7	7	3	7	4	1	1	6	45
1980	1	13	10	6	7	–	–	3	8	48
1981 (Data not available for 1981).										
1982	6	3	9	3	1	4	1	4	8	39
1983	3	8	7	5	3	1	–	5	7	39
1984	5	4	12	1	5	2	–	3	5	37
1985	5	8	14	4	6	3	–	2	11	53
1986	1	6	23	4	2	6	–	1	4	47
Totals	326	246	224	165	140	130	95	94	293	1,713

[a] Argentina, Australia, Austria, Benelux (Holland, Belgium), Brazil, Canada, Iran, Colombia, Hong Kong, Ireland, Luxembourg, Malaysia, Mexico, New Zealand, Philippines, Portugal, Scandinavia (Sweden, Denmark), South Africa, Spain, Zambia, Israel, Pakistan.

Source: Medical Marketing and Media, August, 1983, p.

THE FDA PRE-MARKETING DRUG APPROVAL PROCESS

Before a new drug can be marketed in the U.S., extensive testing must be performed and the FDA must approve the products as being "safe and effective" for its intended uses. Tests begin with animals. If a drug is determined to be safe for limited, controlled clinical trials in humans, a sponsor must submit an Investigational New Drug (IND) application to inform the FDA that efficacy and safety studies in man will be initiated within 30 days unless the FDA objects.

Clinical studies of a new drug in humans are usually divided into three phases. Phase I is an initial, cautious trial in a few healthy persons; Phase II deals with more detailed observations in research subjects who have the disease for which the drug is intended to be effective; Phase III consists of more extensive, often longer tests to ascertain whether the drug is effective for the disease state or syndrome it is intended to treat.

If clinical testing proceeds, substantial record keeping is required throughout the testing period. A sponsor then submits a New Drug Application (NDA) containing documentation of safety and effectiveness studies and manufacturing control procedures to be used in preparing the product.

The attrition rate for prospective new chemical entities as a result of clinical testing is very high. Approximately only one in ten drugs for which INDs are issued go through all clinical phases of investigation. Table 2-10 shows the number of INDs and NDAs filed from 1963 through 1986. The annual number of INDs submitted during this period varied between 671 and 2,112. About half of the INDs submitted are abandoned by the sponsor, usually a pharmaceutical company. Discontinuances usually are based on company evaluations of test results and of the potential of the drug being tested.

PATENT ACTIVITY

Patent activity is another measure of the intensity of pharmaceutical research. A new drug may be the subject of several different patents. Patents may be obtained for new chemical entities, for novel manufacturing processes and for new uses of existing compounds. Tables 2-11, 2-12, and 2-13 show the number of patents issued for drugs and medicines during 1963-1986 and the countries in which the companies that received patents were based. The relative share of patents that were issued for "Drugs and Medicines" to companies based in the U.S. was almost two-thirds from 1963-1972, but declined to 48 percent in 1986.[3]

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[3] The U.S. Patent Office credits patents to the country of residence shown by the inventor on the patent applications.

TABLE 2-8
NEW SINGLE CHEMICAL ENTITY DRUGS INTRODUCED TO U.S. MARKET
BY COUNTRY OF ORIGIN
1940 - 1986

Country of Origin	Solely National Origin (A)	Shared Products (B)[a]	Equivalent Number (C)[b]	Accreditation (A+C)	Percentage of Total 1178 New Drugs
United States	721	10	5.0	726.0	61.6%
Switzerland	78	4	2.0	80.0	6.8
United Kingdom	72	3	1.5	73.5	6.2
West Germany	61	4	2.0	63.0	5.4
France	38	1	0.5	38.5	3.3
Denmark	17	1	0.5	17.5	1.5
Belgium	18			18.0	1.5
Sweden	15	1	0.5	15.5	1.3
Holland	15			15.0	1.3
Japan	20	1	0.5	20.5	1.7
Mexico	9	2	1.0	10.0	0.8
Italy	11	1	0.5	11.5	1.0
Austria	3			3.0	0.3
Canada	3			3.0	0.3
Australia	2			2.0	0.2
Hungary	2			2.0	0.2
Czechoslovakia	1	1	0.5	1.5	0.1
Argentina	1			1.0	0.1
India	1			1.0	0.1
Norway	1			1.0	
Europe (specific nation unknown)	0	1	0.5	0.5	0.0
Source not ascertained	74			74.0	6.3
TOTAL	1163	30	15.0	1178	100.0%

[a] Column B lists the number of drugs for which a country shared the credit with one or more other countries in the origination of a chemical entity.

[b] Equivalent Number (column C) assigns one-half credit for each shared product introduction under column B, i.e., column B divided by two.

Source: PMA Analysis of Paul De Haen data.

TABLE 2-9

NEW SINGLE CHEMICAL ENTITIES INTRODUCED TO U.S. MARKET
BY THERAPEUTIC CLASS
1940-1986

Therapeutic Class	No. in Group	No. in Subgroup	Percentage
Analgesics	35		2.9%
Migraine Therapy		3	
Narcotics		16	
Nonnarcotics		16	
Analeptics	3		0.3
Antagonists and Antidotes	20		1.4
Antagonists		5	
Antidiuretics		2	
Antidotes			
Antineoplastics		11	
Nonspecified		2	
Anesthetics	28		2.4
Inhalants		5	
Injectables		7	
Local and Topical		16	
Anthelmintics	13		1.2
Antiarthritics (nonhormonal)	12		0.8
Anticoagulants	12		1.1
Anticonvulsants	16		1.4
Antihistamines	37		3.2
Anti-infectives	222		18.7
General		1	
Amoebicides		9	
Antibacterials			
General		12	
Urinary		11	
Vaginal		8	
Antibiotics			
Broad and Medium Spectrum		62	
Penicillin and Derivatives		38	
Topical		5	
Unclassified		3	
Antimalarials		8	
Antituberculars		17	
Fungicides--Systemic		8	
Sulfonamides		33	
Antiparasitics		6	
Tropical Diseases--General		1	

TABLE 2-9
(Continued)

NEW SINGLE CHEMICAL ENTITIES INTRODUCED TO U.S. MARKET
BY THERAPEUTIC CLASS
1940-1986

Therapeutic Class	No. in Group	No. in Subgroup	Percentage
Anti-inflammatory Agents (nonhormonal)	15		1.3
Antinauseants	12		1.1
Anti-obesity Preparations	17		1.5
Amphetamines		10	
Other		7	
Antivirals	4		.3
Ataraxics	58		5.0
Bronchodilators	15		1.3
Cancer Chemotherapy	39		3.5
Immunosuppressants	2		0.2
Cardiovascular Preparations	97		7.9
Anti-arrhythmics		10	
Cardiotonics		4	
Hypertensives		7	
Hypotensives		35	
Alkaloids		12	
Vasoconstrictors		1	
Vasodilators			
Coronary		8	
Microcirculatory		2	
Peripheral		9	
Xanthine Derivatives		5	
Other Cardiovasculars		4	
Cholesterol Affecting Agents	13		1.2
Lipotropics		3	
Other		10	
Coagulants	4		0.4
Convulsants	1		0.1
Cough and Cold Preparations	24		2.1
Cough Preparations		12	
Nasal Decongestants		12	
Dermatologic Preparations	53		4.6
Antipruritics			
Local		3	
Systemic		2	
Corticoids--Local		17	
Fungicides--Topical		19	
Other		12	
Diabetic Therapy	12		0.9
Hypoglycemics		11	
Hyperglycemics		1	
Diuretics	38		3.4
Benzothiazides		11	
Other		27	

TABLE 2-9
(Continued)

NEW SINGLE CHEMICAL ENTITIES INTRODUCED TO U.S. MARKET
BY THERAPEUTIC CLASS
1940-1986

Therapeutic Class	No. in Group	No. in Subgroup	Percentage
Enzymes	9		0.8
Eye Preparations	17		1.4
Fertility Agents (nonhormonal)	1		0.1
Gastrointestinal Preparations	73		6.3
Antacids		9	
Antidiarrheals		5	
Antispasmodics		37	
Biliary Tract Therapy		3	
Enemas		2	
Enzymes--Digestive		1	
Laxatives		6	
Other G.I. Preparations		10	
Hematinics	15		1.3
Hemostatics	2		0.2
Hormones	91		8.0
ACTH		2	
Corticoids		33	
Anabolics (Hormonal)		9	
Androgens		6	
Estrogens		21	
Progesterones		11	
Other Hormones		9	
Hospital Solutions	6		0.5
Muscle Relaxants	38		3.3
General		16	
Parkinsonism		12	
Surgical		10	
Oxytocics	5		0.4
Parasympathomimetics	6		0.5
Psychostimulants	22		1.9
Sedatives and Hypnotics	22		2.0
Barbiturates		6	
Nonbarbiturates		16	
Thyroid Therapy	9		0.7
Thyroid Preparation		5	
Antithyroid Preparations		4	
Vitamins and Nutrients	16		1.4
Vitamins		10	
Nutrients		6	
Unclassified	44		3.0
TOTAL	1178		100.0%*

*May not add due to rounding.
Source: PMA Analysis of Paul De Haen data.

TABLE 2-10

NEW DRUG FILINGS WITH FOOD AND DRUG ADMINISTRATION
1963-1986

Year	Original INDs Submitted	INDs Discontinued by Sponsor	Original NDAs Submitted	NDAs Approved	New Molecular Entities*
1963	1066	6	192	71	16
1964	875	215	160	70	20
1965	761	306	221	50	13
1966	715	580	216	50	17
1967	671	627	128	74	16
1968	859	564	108	56	11
1969	956	482	60	39	11
1970	1127	N.A.	87	53	11
1971	923	1167	256	68	14
1972	902	452	272	42	10
1973	822	311	149	77	14
1974	802	399	129	95	23
1975	876	472	137	68	15
1976	855	524	127	101	23
1977	925	802	124	63	21
1978	925	588	121	86	22
1979	940	539	182	94	14
1980	1087	626	162	114	12
1981	1184	353	129	96	27
1982	1467	689	202	116	28
1983	1798	N.A.	269	94	14
1984	2112	N.A.	217	142	22
1985	1904	N.A.	148	100	30
1986	1623	N.A.	120	98	20

* FDA's definition of new molecular entities differs from the definition of new chemical entities by Paul De Haen, Inc., a key source for PMA's analysis of new drug introductions and the one used in this book. PMA omits diagnostic agents, although the FDA count of new molecular entities includes these agents. In addition, FDA uses application approval dates, whereas De Haen and PMA use year of introduction to the market. Thus, new molecular entities indicated here for a given year may be based on INDs and NDAs submitted a year or more earlier.

N.A.: Not Available.

Source: Unpublished data, Bureau of Drugs, Food and Drug Administration, U.S. Department of Health and Human Services. New Drug Evaluation Project, Briefing Book, FDA, May 1982, September 1983, March 1986.

TABLE 2-11
NUMBER OF NEW U.S. PATENTS FOR
DRUGS AND MEDICINES
BY ORIGIN
1963 - 1986

	NUMBER OF PATENTS															
	1963-1972	1973	1974	1975	1976	1977	1978	1979	1980	1981	1982	1983	1984	1985	1986	TOTAL
TOTAL	8865	1278	1524	1841	2284	2407	2378	1826	2454	2575	2223	1996	2475	2489	2504	39119
U.S. ORIGIN	5776	744	835	1051	1201	1221	1239	917	1211	1313	1043	939	1270	1234	1198	21192
FOREIGN ORIGIN	3089	534	689	790	1083	1186	1139	909	1243	1262	1180	1057	1205	1255	1306	17927
U.S. ORIGIN	5776	744	835	1051	1201	1221	1239	917	1211	1313	1043	939	1270	1234	1198	21192
U.S. CORP. OWNED	5152	664	729	931	1105	1103	1125	823	1057	1154	904	802	1102	1097	1035	18783
U.S. GOVT. OWNED	122	26	23	31	25	25	17	18	33	27	26	28	32	27	27	487
U.S. INDIV. OWNED	480	50	79	81	58	85	90	69	111	123	99	98	125	100	118	1766
FOREIGN OWNED	22	4	4	8	13	8	7	7	10	9	14	11	11	10	18	156
FOREIGN ORIGIN	3089	534	689	790	1083	1186	1139	909	1243	1262	1180	1057	1205	1255	1306	17927
U.S. OWNED	517	79	120	116	157	166	164	140	183	145	145	120	107	142	133	2434
FOREIGN OWNED	2572	455	569	674	926	1020	975	769	1060	1117	1035	937	1098	1113	1173	15493
FOREIGN CORP.	2308	387	492	618	870	965	918	720	993	1034	952	878	1015	1040	1095	14285
FOREIGN GOVT.	2	1	2		1	2	4	2	4	2	17	13	18	10	9	87
FOREIGN INDIV.	262	67	75	56	55	53	53	47	63	81	66	46	65	63	69	1121

Source: U.S. Patent and Trademark Office

TABLE 2-12
PERCENTAGE OF U.S. PATENTS FOR
DRUGS AND MEDICINES
BY ORIGIN
1963 - 1986

	NUMBER OF PATENTS															
	1963-1972	1973	1974	1975	1976	1977	1978	1979	1980	1981	1982	1983	1984	1985	1986	TOTAL
TOTAL	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100
U.S. ORIGIN	65	58	55	57	53	51	52	50	49	51	47	47	51	50	48	54
FOREIGN ORIGIN	35	42	45	43	47	49	48	50	51	49	53	53	49	50	52	46
U.S. ORIGIN	65	58	55	57	53	51	52	50	49	51	47	47	51	50	48	54
U.S. CORP. OWNED	58	52	48	51	48	46	47	45	43	45	41	40	45	44	41	48
U.S. GOVT. OWNED	1	2	2	2	1	1	1	1	1	1	1	1	1	1	1	1
U.S. INDIV. OWNED	6	4	5	4	3	4	4	4	5	5	4	5	5	4	5	5
FOREIGN OWNED	*	*	*	*	1	*	*	*	*	*	1	1	*	1	1	*
FOREIGN ORIGIN	35	42	45	43	47	49	48	50	51	49	53	53	49	50	52	46
U.S. OWNED	6	6	8	6	7	7	7	8	7	6	7	6	4	6	5	6
FOREIGN OWNED	29	36	37	37	40	42	41	42	43	43	46	47	44	45	47	40
FOREIGN CORP.	26	30	32	34	38	40	39	39	40	40	43	44	41	42	44	37
FOREIGN GOVT.	*	*	*	0	*	*	*	*	*	*	*	1	1	*	*	*
FOREIGN INDIV.	3	6	5	3	2	2	2	3	3	3	3	2	2	3	3	3

* Less than one percent.
Source: U.S. Patent and Trademark Office

TABLE 2-13
NUMBER OF FOREIGN ORIGIN PATENTS FOR
DRUGS AND MEDICINES
BY COUNTRY
1963-1986

	NUMBER OF PATENTS				
COUNTRY OR ORIGIN	1963-1972	1973-1977	1978-1982	1983-1986	TOTAL
West Germany	682	1063	1324	1004	4073
Japan	513	827	1239	1371	3950
United Kingdom	344	548	885	669	2446
France	426	549	615	484	2074
Switzerland	415	443	492	287	1637
Italy	143	174	301	307	925
Canada	101	137	138	113	489
Netherlands	110	62	104	65	341
Mexico	22	21	5	11	59
Sweden	85	117	115	54	371
Belgium	47	49	110	66	272
Hungary	15	35	100	116	266
Denmark	35	30	34	47	146
U.S.S.R.	10	44	37	28	119
Austria	29	31	33	18	111
Other Countries	112	152	201	183	648
TOTAL	3089	4282	5733	4823	17,927

Source: U.S. Patent and Trademark Office

The pharmaceutical industry is the major source in the U.S. for discovering and developing drug products, and patent protection provides necessary incentives to stimulate investment of millions of dollars in research and development. By providing inventors with an exclusive right for 17 years to sell these inventions in the U.S., patents enable companies to realize adequate returns on their substantial investments. New medicines help to improve the health of people in this country and, therefore, great social benefits result from the patent protection given to the inventors of these products. Patents also stimulate additional research by providing useful data for other research efforts.

A patent application is usually filed as soon as a chemical compound shows promising pharmacological activity. Extensive testing is usually required, however, to determine whether a compound can be developed for practical use as a medicine. Such testing in animals and man - and processing through the IND and NDA phases - often continues for years after a patent has been granted. This reduces the patent-protected marketing time during which a company may recover its investment in the product.

CHAPTER III

THE VALUE OF PHARMACEUTICALS IN IMPROVING HEALTH CARE AND IN REDUCING COSTS OF ILLNESS

Pharmaceutical research helps to improve the health of the population. Decreased morbidity and increased longevity are key measures for such progress. Numerous economic studies document that drugs are a cost-effective form of therapy that can substantially reduce health care costs.

MORBIDITY

Since 1940, the use of drugs and vaccines has substantially reduced the incidence of certain diseases. For example, drug therapy has virtually eliminated diphtheria and polio (Table 3-1).

TABLE 3-1

REDUCTION IN REPORTED U.S. CASES OF SELECTED DISEASES
1940 AND 1985

Disease	1940	1985	Percent Reduction	Form of Treatment or Prevention
Diphtheria	15,536	2	99.9%	Vaccines
Measles	291,162	2,700	99.1	Vaccines
Polio	57,879*	5	99.9	Vaccines
Syphilis	472,900	70,000**	85.2	Antibiotics
Tetanus	486	71	85.4	Vaccines
Tuberculosis	102,984	21,800	78.8	Anti-infectives
Typhoid Fever	9,809	384	96.1	Vaccines & Antibiotics
Whooping Cough	183,866	3,300	98.2	Vaccines

* This figure is for 1952; three years before Salk vaccine was introduced.
** 1984
Source: Statistical Abstracts, (various years), U.S. Department of Commerce.

Reduction in morbidity--sickness and sick days--has been achieved for other forms of illness. For example, drug therapy has dramatically reduced the number of patients who require hospitalization for tuberculosis. The disease is now treatable at home with para-aminosalicylic acid (PAS), isoniazid, streptomycin, rifampin, and other drugs. A similar result has been achieved through the use of H_2 antagonist drugs for ulcers. Besides reducing the need for hospitalization, drugs also prevent and cure disease, supplement other medical treatment such as surgery, and restore patients to a normal life.

MORTALITY

Medicines also have enabled people to lead longer, healthier lives, as shown by the substantial improvement in mortality rates (Table 3-2). Since 1940, life expectancy has increased by 17.3 percent for men and by 20.1 percent for women (Table 3-3).

COST-EFFECTIVENESS

Studies sponsored by PMA show that drugs not only reduce sickness and save lives, but they also save money. Three studies of cardiovascular beta-blocker drugs show that their benefits far exceed their costs. In preventing second heart attacks, these drugs may save $1.6 billion to $3.0 billion a year.[1] As an alternative to surgery for treating glaucoma, use of a beta-blocker may save $746 million to $1.06 billion annually.[2] In treating angina, use of beta-blockers may save as much as $237 million a year.[3]

TABLE 3-2

MORTALITY: REDUCTIONS IN U.S. DEATHS PER 100,000 POPULATION FROM SELECTED DISEASES 1960 and 1985

Disease	1960	1985	Percent Reduction
Rheumatic Fever and Rheumatic Heart Disease	10.3	2.6	74.8%
Hypertensive Heart Disease	37.0	8.6	76.8
Hypertension	7.1	3.1	56.3
Cerebrovascular Disease	108.0	64.0	40.7
Atherosclerosis	20.0	9.9	50.5
Pneumonia and Influenza	37.3	27.9	25.2
Asthma	3.0	1.6	46.7
Ulcer of Stomach & Duodenum	6.3	2.8	55.6
Infections of Kidneys	4.3	.8	81.4
Tuberculosis (all forms)	6.1	.7	88.5
Meningitis	1.3	.5	61.5

Source: Statistical Abstract, (1986), U.S. Department of Commerce.

[1] Beta Blocker Reduction of Mortality and Reinfarction Rate in Survivors of Myocardial Infarctions: A Cost-Benefit Study, A.D. Little, Inc. (1984).

[2] Use of a Beta Blocker in the Treatment of Glaucoma: A Cost-Benefit Study, A.D. Little, Inc. (1984).

[3] Use of Beta Blockers in the Treatment of Angina: A Cost-Benefit Study, A.D. Little, Inc. (1984).

TABLE 3-3

U.S. EXPECTATION OF LIFE AT BIRTH
1920-1986

Year	Men	Women	Average
1920	53.6	54.6	54.1
1930	58.1	61.6	59.7
1940	60.8	65.2	62.9
1950	65.6	71.1	68.2
1960	66.6	73.1	69.7
1965	66.8	73.7	70.2
1966	66.7	73.8	70.1
1967	67.0	74.2	70.5
1968	66.6	74.0	70.2
1969	67.0	74.3	70.5
1970	67.1	74.8	70.9
1971	67.4	74.8	71.0
1972	67.4	75.2	71.2
1973	67.6	75.3	71.3
1974	68.1	75.8	71.9
1975	68.7	76.5	72.5
1976	69.0	76.7	72.8
1977	69.3	77.1	73.2
1978	69.4	77.3	73.3
1979	70.0	77.3	73.9
1980	70.0	77.5	73.7
1981	70.4	77.9	74.2
1982	70.9	78.2	74.6
1983	71.0	78.1	74.6
1984	71.2	78.2	74.7
1985	71.2	78.2	74.7
1986*	71.3	78.3	74.9

* Preliminary data.

Source: Statistical Abstract (1985), U.S. Department of Commerce. 1983 Life Insurance Fact Book, Telephone Conversations, National Center for Health Statistics.

Another study demonstrates the cost-effectiveness of vaccines against measles, mumps, rubella, pneumococcal pneumonia in high-risk groups, pertussis, adenoviral respiratory infections, polio, and influenza in the elderly.[4] For example, the study reports that the benefits of measles vaccine were more than ten times the costs over a nine-year period.

[4] Benefits and Costs of Human Vaccines in Developed Countries: An Evaluative Survey, Weisbrod and Huston (1984).

A review of the literature[5] also shows the cost-effectiveness of drug therapy. In a study of the preventive use of an antibiotic, for example, the average annual cost of preventing urinary tract infections was found to be $85 per patient, compared to $126 for treating the infection--a savings of 33 percent. In another study, Medicaid expenditures were determined to be approximately 70 percent less for persons using a new anti-ulcer drug than for those not receiving the medicine. And a third study concluded that treating mental patients with an anti-psychotic drug was the least costly of five forms of therapy--lower by 26.1 percent to 62 percent--and was one of the most effective methods of treatment.

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[5] Economic Evaluations of Medicines: A Review of the Literature, Judith L. Wagner (1984).

CHAPTER IV

TODAY'S HEALTH CARE ENVIRONMENT

The provision of health services and products is a major industry in the United States: expenditures for these goods and services represent over one-tenth of total annual spending for all goods and services. The rate of growth of these expenditures continues to outpace that of the gross national product (GNP).

Despite this growth in overall expenditures, the proportion of health expenditures for non-hospital drugs and medical sundries[1] has been declining and now represents only 6.7 percent of total health care expenditures. The relative cost of drugs, in other words, is shrinking in comparison with other medical expenditures.

NATIONAL HEALTH EXPENDITURES

The nation spent $458 billion for health care in 1986, an average of $1,837 per person. During the past 50 years, the health care industry has steadily expanded its share of the GNP, from 3.5 percent in 1929 to 10.9 percent in 1986 (Table 4-1).

Table 4-2 shows the major components of national health expenditures. Hospital care represents the largest category of health expenditures: in 1986, hospitals accounted for $180 billion, nearly 40 percent of all health care costs.

While total health expenditures have increased steadily over the last 25 years, drugs and medical sundries have consistently declined from 12.4 percent of national health expenditures in 1965 to 6.7 percent in 1986 (Table 4-3).

In recent years, general inflation in the economy as a whole has been the most important cause of increasing health care expenditures. Between 1980 and 1986, general inflation accounted for 47 percent of health care expenditure growth, increased services per capita accounted for 26 percent, population growth caused 10 percent, and excess health care sector inflation was

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[1] The category "Drugs and Medical Sundries" is used by the U.S. Health Care Financing Administration as a subcategory of health expenditures and is derived in part from U.S. Department of Commerce calculations of personal consumption expenditures. The term encompasses prescription and over-the-counter drugs and sundries. This total does not include hospital drug expenditures. Prescription drugs are estimated to account for 57 percent of the total spent on drugs and medical sundries, according to the Health Care Financing Administration.

TABLE 4-1

NATIONAL HEALTH EXPENDITURES, AGGREGATE, PER CAPITA
AND PERCENT OF GROSS NATIONAL PRODUCT
Calendar Years 1929-1986
(Current $)

Year	Gross National Product (in billions)	Health Expenditures		
		Amount (in billions)	Per Capita	Percent of GNP
1929	$ 103.40	$ 3.60	$ 29.00	3.6%
1940	100.00	4.00	30.00	4.0
1950	286.50	12.70	82.00	4.4
1955	400.00	17.70	105.00	4.4
1960	506.50	26.90	146.00	5.3
1965	705.00	41.90	205.00	5.9
1966	756.00	46.30	225.00	6.1
1967	816.00	51.50	248.00	6.3
1968	873.40	58.20	278.00	6.7
1969	944.00	65.60	310.00	7.0
1970	1,015.00	75.00	349.00	7.4
1971	1,097.60	83.50	386.00	7.7
1972	1,185.90	93.90	429.00	7.9
1973	1,326.40	103.40	468.00	7.8
1974	1,434.20	116.30	522.00	8.1
1975	1,598.00	132.70	590.00	8.3
1976	1,718.00	150.80	665.00	8.5
1977	1,918.30	170.20	743.00	8.9
1978	2,163.90	189.70	822.00	8.4
1979	2,417.80	214.70	920.00	8.6
1980	2,732.00	248.10	1,054.00	9.1
1981	3,053.00	287.00	1,207.00	9.4
1982	3,166.00	323.60	1,348.00	10.2
1983	3,402.00	357.20	1,473.00	10.5
1984	3,765.00	391.10	1,597.00	10.4
1985	3,998.00	422.60	1,710.00	10.6
1986	4,206.00	458.20	1,837.00	10.9

Source: HCFA, Health Care Financing Review, Fall 1986. HHS News (press release), U.S. Department of Health and Human Services, June 23, 1987.

TABLE 4-2

PERCENT DISTRIBUTION OF TOTAL NATIONAL HEALTH EXPENDITURES
BY TYPE OF EXPENDITURE
Calendar Years 1965, 1975, 1986

Type of Expenditure		Calendar Year 1965		Calendar Year 1975		Calendar Year 1986
TOTAL (Billions of Current Dollars)		$ 41.9		$132.7		$458.2
TOTAL (Percent)		100.0%		100.0%		100.0%
Health Services & Supplies		91.6		93.7		96.5
Personal Health Care Expense	85.7		88.0		88.2	
Hospital Care	33.4		39.3		39.2	
Physicians' Services	20.3		18.8		20.1	
Dentists' Services	6.7		6.2		6.5	
Other Professional Services	2.4		2.0		3.1	
Drugs & Medical Sundries	12.4		9.0		6.7	
Eyeglasses & Appliances	2.9		2.4		1.8	
Nursing Home Care	5.0		7.6		8.3	
Other Health Services	2.6		2.8		2.6	
Program Administration and Net Cost of Health Insurance	4.1		3.3		5.3	
Government Public Health Activities	1.9		2.4		2.9	
Research & Medical Facilities Construction		8.4		6.3		3.6
Research		3.6		2.5		1.8
Construction		4.8		3.8		1.8

Source: HCFA, Health Care Financing Review, Fall, 1986. PMA Calculations. HHS News (press release), U.S. Department of Health and Human Services, June 23, 1987. PMA calcuations.

TABLE 4-3

DRUGS AND MEDICAL SUNDRIES
AS A PERCENT OF NATIONAL HEALTH EXPENDITURES

Year	Ratio
1965	12.4%
1966	11.9
1967	11.3
1968	11.0
1969	10.8
1970	10.7
1971	10.3
1972	9.9
1973	9.8
1974	9.5
1975	9.0
1976	8.7
1977	8.3
1978	8.1
1979	8.0
1980	7.6
1981	7.2
1982	6.9
1983	6.9
1984	6.8
1985	6.8
1986	6.7

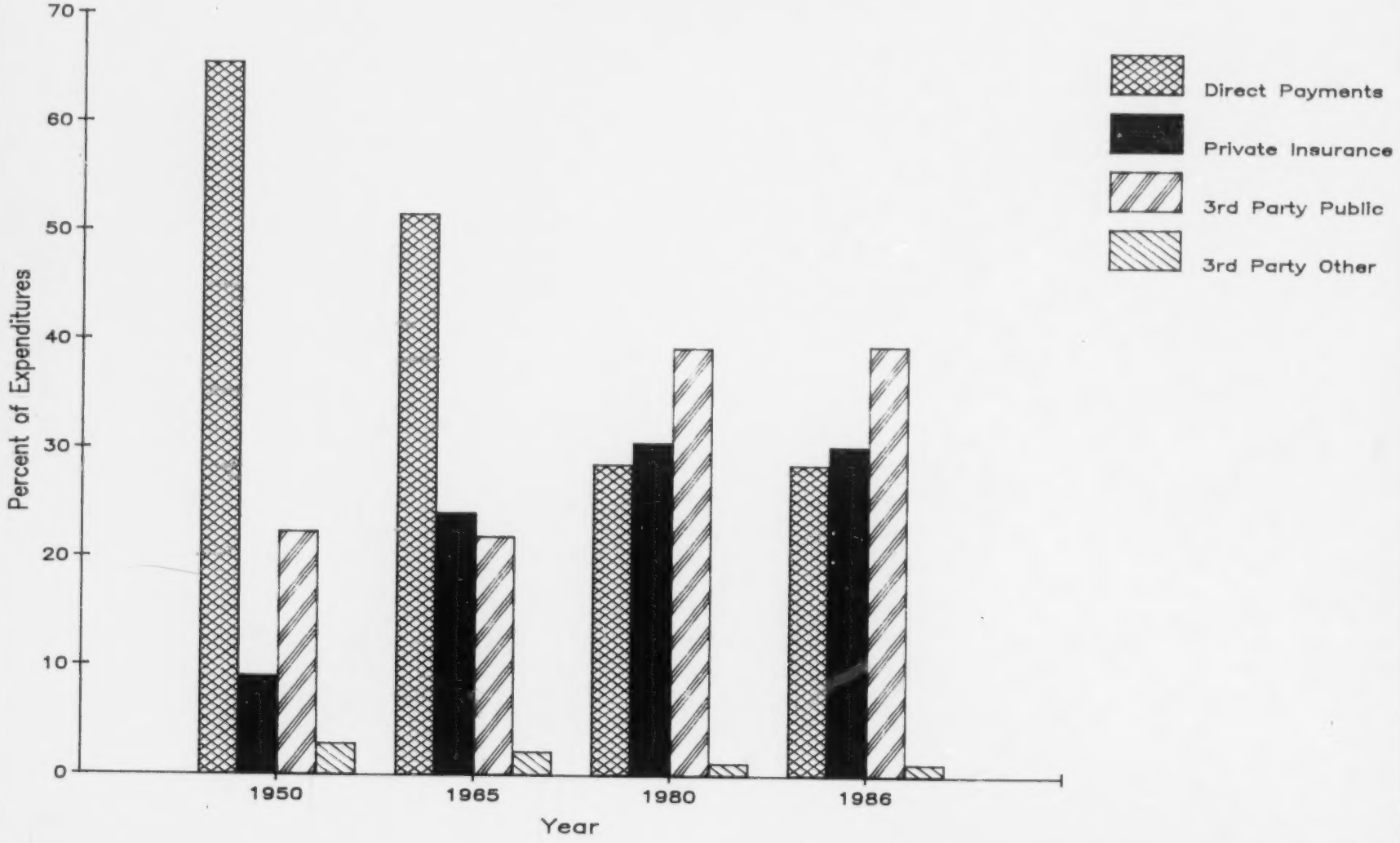
Source: Health Care Financing Administration.

responsible for 17 percent. With inflation declining over this period, however, increased services became the leading source of increased health expenditures in 1986.

The increase in expenditures due to services per capita and health sector inflation has come largely as a result of health insurance coverage. Private insurance covers 79 percent of the U.S. population for hospitalization; more than 85 percent of the population has private health insurance or is eligible for public programs that provide some financial protection against health care costs. In recent years, the percentage of the population with health insurance has stabilized and may be declining slightly.

Insurance coverage has greatly affected the distribution of health care payments among consumers, private insurers, and the government (Figure 4-1). In 1950, direct out-of-pocket payments by consumers accounted for 65.5 percent of all personal health care expenditures. By the end of 1986, consumers were paying only

Figure 4-1
Personal Health Care Expenditures
By Source of Funds
Selected Calendar Years



Source: Health Care Financing Administration

28.7 percent of their health care bills, with insurers paying the balance. Over the same period, public financing increased from 22.4 percent of personal health care expenditures in 1950 to 39.6 percent in 1986. Since 1980, however, these percentages have changed only slightly.

HEALTH CARE PROFESSIONS PERSONNEL AND FACILITIES

Health Care Professions Personnel. The number of people employed in the health care industry has grown as a result of increased demand for services and the greater intensity of care provided. Health care employment grew from 4.2 million in 1970 to 7.9 million in 1985, an increase of over 88 percent.

Registered nurses are the largest health care occupational group, with 1.4 million members in 1985. Nursing aides are the second largest group, with 1.2 million members (Table 4-4).

Between 1970 and 1980, the number of active medical and osteopathic physicians grew by 40 percent to 457,500. As a result, there were 19.7 physicians per 10,000 population in 1980, a significant increase from 1950 when there were 14.1 physicians per 10,000 population. By 1986, the total number of physicians was over 504,000 which represents 20.4 physicians per 10,000 population.

TABLE 4-4

U.S. HEALTH INDUSTRY PERSONNEL
SELECTED CATEGORIES
1986

Occupation	Personnel
Doctors of Medicine	504,000 (a)
Doctors of Osteopathy	21,000 (a)
Dentists	163,000 (a)
Pharmacists	158,000 (a)
Health Technologists and Technicians	1,112,000 (b)
Optometrists	18,000 (a)
Physician Assistants	43,000 (c)
Registered Nurses	1,447,000 (b)
Practical Nurses	402,000 (b)
Nursing Aides	1,242,000 (b)
Managers, Medicine and Health	106,000 (b)

Sources: (a) Business Mailers, Inc., 1986 data.
(b) 1987 Statistical Abstract of U.S., 1985 data.
(c) 1984 data.

Facilities. In the United States, most medical care is provided in hospitals. In 1873, the U.S. Bureau of Education listed 178 hospitals in the first survey of health care facilities. In 1985, there were 5,732 community hospitals (Table 4-5) with approximately one million beds. These hospitals admitted 33 million patients, provided 219 million outpatient services, employed approximately three million people and spent $130 billion in 1985, an increase in spending of 5.7 percent over 1984. Over 5,000 hospitals have their own pharmacies.

Other types of health care facilities are listed in Table 4-5. The number of nursing homes has increased as a result of an increase in the size of the elderly population, changes in family living arrangements, and public financing of health care for the elderly.

Outpatient and home care will play an increasingly important role in coming years. The number of Medicare certified home health agencies has increased from 1,019 in 1966, largely because they began to receive Medicare and Medicaid funding for the services they provide.

TABLE 4-5
SELECTED U.S. HEALTH CARE ESTABLISHMENTS AND SUPPLIERS
1985

Type of Facility		Number
Hospitals (TOTAL)		6,872
Community (Short Term)		5,732
Not-for-Profit (Nongovernment)	3,349	
For-Profit	805	
State and Local Government	1,578	
Noncommunity (e.g., Federal, Long-Term General, and psychiatric)		1,140
Not-for-Profit (Nongovernment)	180	
For-Profit	247	
State and Local Government	318	
Federal Government	343	
Hospital Units of Institutions	52	
Nursing Homes (25 or more beds)[a]		14,567
Skilled Nursing Facility Only (SNF)	3,000	
Combined Skilled Nursing & Intermediate Care Facilities	4,400	
Intermediate Care Facility (ICF)	5,100	
SNFs, ICFs, and Combinations not participating in Medicaid or Medicare	2,100	
Home Health Agencies (Medicare-Certified)		5,317
Pharmacies		68,304

[a] This total is a 1980 figure. The total was distributed by type using 1977 breakdown. Figures do not add to total because of rounding.

Sources: Hospitals: AHA, Hospital Statistics, (1986 edition).
Nursing Homes: NCHS, 1977 National Nursing Home Survey; NCHS, Trends in Nursing and Related Care Homes and Hospitals; PMA estimates.
Home Health Agencies: National Association for Home Care.
Pharmacies: Business Mailers, Inc., 1986 figures.

THE ROLE OF GOVERNMENT IN HEALTH CARE

Since the mid-1960s, government has played a key role in the growth and development of the health care system--largely through direct financing of services and regulation of the health care system.

Public Financing of Health Care: The Medicare and Medicaid Programs. Of most importance, government programs were created to provide financing for health facilities, products, and services. By greatly increasing the resources available to the health care industry and changing the pattern of demand, these programs have affected both the volume and mix of services provided. In 1965 public expenditures represented 26 percent of the total national health bill of $41.7 billion. By 1986, public funds accounted for 41.4 percent of total national expenditures of $458 billion.

Two federal programs, Medicare and Medicaid, are primarily responsible for the increases in public health care expenditures. Enacted in 1965 as amendments to the Social Security Act, these programs were designed to enable the elderly and the poor to obtain needed health services.

The Medicare program provides health insurance for persons 65 and older, and for certain people under 65 who are chronically ill or disabled. Part A of the program provides hospital insurance for all eligible beneficiaries. Part B provides insurance for physicians' services and certain other non-hospital services and is available to eligible beneficiaries for a relatively small monthly premium. More than 30.0 million persons are currently enrolled under Medicare, 90 percent of whom are 65 or older. In 1986, payments for Medicare benefits totaled $76.0 billion.

The Medicaid program, run in partnership with participating states, provides payments for medical care for low-income individuals and families. All people who receive cash payments under welfare programs such as Aid to Families with Dependent Children and the Supplemental Security Income program are eligible for Medicaid under federal law. States may extend benefits to other categories of people in addition to the beneficiaries mandated by federal law. Many states provide benefits to the "medically needy" as well as to the federally-mandated groups.

Certain basic services must be offered in any state Medicaid programs, such as inpatient hospital care, outpatient hospital services, laboratory and x-ray services, skilled nursing facility services, family planning services, and physician services. States may also provide additional benefits if they elect to do so, including prescription drugs, eyeglasses, and inpatient psychiatric care.

The Medicaid program is state-administered and costs are shared by participating states and the federal government. In 1986, Medicaid paid $43.6 billion in medical benefits for acute health care and long term care for roughly 22 million recipients, an 8.7 percent increase over 1985. Hospital services, usually the largest category of expense, accounted for 36.2 percent of total Medicaid expenditures. Expenditures for nursing home care, for the first time, equalled hospital expenditures, and physicians' services represented 8.9 percent. Retail pharmacy sales of prescription drugs and medical sundries accounted for 6.7 percent of 1986 health care expenditures under Medicaid, or about $2.9 billion (Figure 4-2).

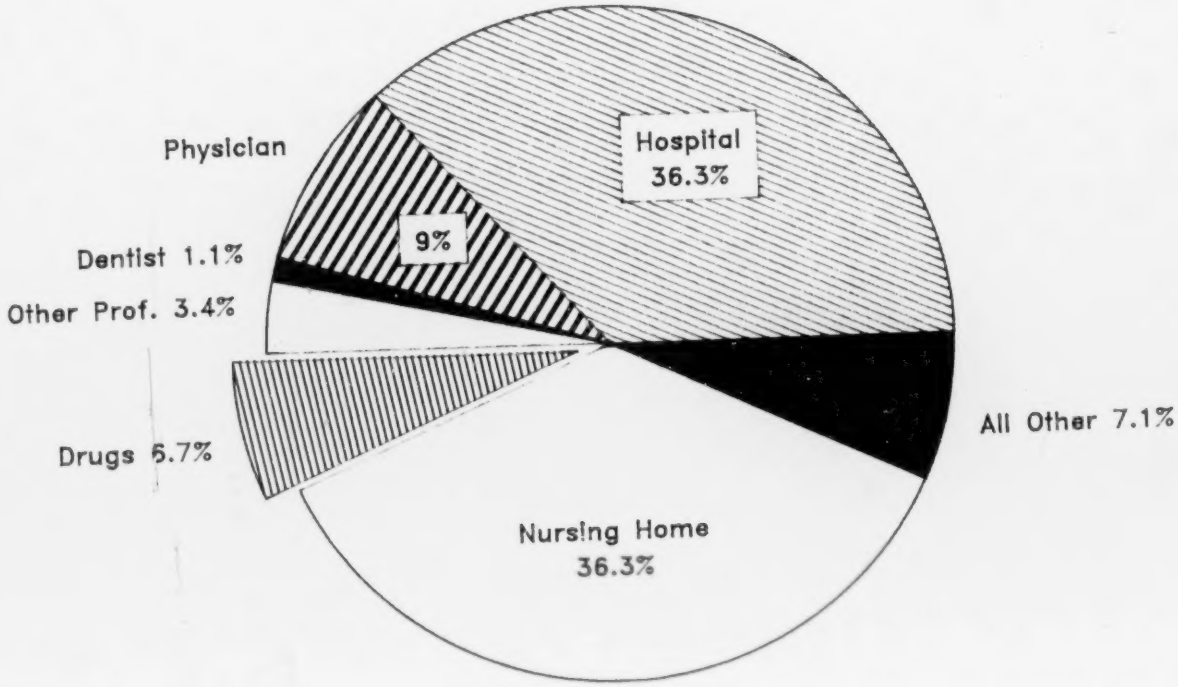
In addition to Medicare and Medicaid, the federal government provides health care benefits for specific beneficiary groups such as military personnel and their dependents, veterans, and Native Americans. In fiscal years 1982 and 1983, block grants were introduced to consolidate federal spending in areas such as disease prevention and maternal and child health.

Cost Containment and Regulation. During the decade ending in 1986, national health expenditures grew at an annual rate of 11.8 percent, increasing from $150.8 billion in 1976 to $458 billion in 1986. During the same period, the consumer price index increased by 6.6 percent annually and the gross national product by 9.4 percent.

In response to this increase in health care expenditures, government at all levels initiated measures to keep costs within acceptable limits. Government efforts to restrain costs have focused on the controllable elements in this list: medical care price inflation in excess of general inflation, and increases in utilization of services and intensity of care. However, recent data suggest that lower increases in health expenditures are due primarily to lower rates of inflation rather than decreases in these controllable elements. The growth rate in expenditures attributable to utilization and intensity increased from 1.7 percent in 1984 to 2.6 percent in 1985, and rose again to 3.0 percent in 1986. During the same period, the rate of growth attributable to general inflation declined from 4.0 percent to 2.8 percent.

Since 1972, federal and state governments have taken many steps to become "prudent buyers" of health care services, and have imposed regulatory limits on the health care system. In 1972, Congress established the Professional Standards Review Organization (PSRO) program, mandating review of Medicare hospital admissions to assure quality of care and reduce utilization. In 1974, the National Health Planning and Resources Development Act revised and strengthened state and local health planning. The planning agencies sought to restrain expenditure growth by limiting the construction of excess capacity while ensuring that adequate services were available. The available evidence indicates that they were unable to forestall excess capacity.

Figure 4-2
Medicaid Expenditures for Health Services and Supplies
Percentages by Type of Service
Calendar 1986



Source: Health Care Financing Administration

Numerous other actions were taken to restrain expenditure growth including state regulation of hospital rates, limitation of hospital Medicare and Medicaid reimbursement, and restriction of payment to other providers. In the case of drugs, DHHS promulgated Maximum Allowable Cost (MAC) regulations limiting the price at which a drug is widely and consistently available." States have initiated or considered other programs to reduce Medicaid drug expenditures. These include capitation payment of pharmacies, restriction of drug choice to products on a state-established formulary, drug utilization review, and volume purchasing plans. Although there has been no comprehensive analysis of the impact of the MAC program and only limited analysis of the impact of other programs, the Health Care Financing Administration recently published new regulations for Medicaid drug reimbursement. The new reimbursement limits established under these regulations will apply to a state's aggregate expenditures rather than to specific drugs. The effectiveness of all these alternatives for restraining Medicaid costs remains uncertain.

Hospital care is the single largest component of national health expenditures. With an annual growth rate of 11.4 percent during the ten years ending in 1986, hospital costs grew more rapidly than any category other than nursing home costs. In 1983, Congress responded by radically revising the way in which Medicare pays hospitals. Instead of reimbursing hospitals for their costs, Medicare now pays a prospectively determined price for each admission. The fixed price for each patient stay is determined by the diagnostic classification. This approach is intended to encourage hospitals to adopt cost-reducing strategies.

APPENDIX
KEY SOURCES OF DATA

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